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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 49

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

GODFREY HAMMEL AND PEARL HAMMEL

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITION FOR CERTIORARI FILED APRIL 10, 1940

CERTIORARI GRANTED MAY 20, 1940

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Dec. 30—Memorandum opinion rendered, Ernest H. Van Fossan, Div. 9. Judgment will be entered for the petitioner.
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1938

Mar. 24—Petition for review by U. S. Circuit Court of Appeals (6) with assignments of error filed by General Counsel.
Apr. 4—Proof of service filed by General Counsel. (2) Attorney and taxpayer.
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Before United States Board of Tax Appeals

Petition

Filed August 10, 1936

The above-named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency IT:AR:D-1 LB-90D dated May 13, 1936, and as a basis for this proceeding allege as follows:

(1) The petitioners are individuals, husband and wife, living together and filed a joint income-tax return for the calendar year 1934. The address is 1248 Free Press Building, Detroit, Michigan.

(2) The notice of deficiency, a copy of which is hereto attached marked Exhibit A, was mailed to the petitioners on May 13, 1936.

(3) The taxes in controversy are income taxes for the calendar year 1934 and amount to $426.79.

ERRORS

The determination of the tax set forth in the said notice of deficiency is based upon the following errors.

(4) The Commissioner errs when he contends that only $2,000.00 is allowable as a deduction of the loss of $4,998.03 claimed because of one of the petitioners (Pearl Hammel) loss of her investment in a land syndicate thru foreclosure.

(4a) The Commissioner errs when he contends that a loss arising out of a sheriff's foreclosure sale is a capital loss from "sale or exchange" within the intent and meaning of Sec. 117 of the Revenue Act of 1934 and therefore is subject to the limitations on losses under Sec. 117-D.

FACTS

The facts upon which the petitioners rely as a basis for this proceeding are as follows:

(5) Mrs. Pearl Hammel, one of the petitioners, made a speculative investment of $4,998.03 (this is the amount of actual cash invested) in a land syndicate, which syndicate was purchasing a piece of acreage (about 80 acres) on land contract for the prime purpose of selling same at an advance price over cost. At the time of foreclosure there was due and owing the vendor on this property an unpaid balance of around $80,000.00 plus accrued interest and
4 accrued and unpaid State and County Taxes totaling about $15,000.00 making the total unpaid balance approximately $95,000.00.

(6) Foreclosure proceedings were started in Oakland County Circuit Court and a deficiency judgment was granted against the petitioner, Mrs. Pearl Hammel, in the amount of $89,000.00. Around the 1st of April 1934 the Oakland County Sheriff made the "sheriff sale" and dispossessed the petitioner, Pearl Hammel, of any and all of her right, title and/or interest in this property.

(7) Petitioner, Pearl Hammel, was insolvent and in order to wipe out the deficiency judgment of $89,000.00 against her she filed a petition in bankruptcy in the District Court of the United States, Eastern District of Michigan on the 26th day of April 1934, No. 17315, and was duly adjudged bankrupt.

PRAYER

The petitioners pray for relief from the deficiency asserted by the respondent and rely upon the following particulars.

(8) The total loss of her investment of $4,998.03 was due to the fact that she was dispossessed of her interest in this property by due process of law and should be allowed as a deduction in full for a worthless investment under Sec. 23 Revenue Act of 1934, and Art. 23, E–1 (b), E–4, and K–4, Reg. 86. That she was not a party to a sale or exchange transaction, therefore, the loss is not limited to the provisions of Sec. 117 (d).

Petitioners pray that the Board may hear and redetermine the deficiency herein alleged.

Petitioners pray that the Board may advance this case and have it immediately placed upon its circuit calendar to be heard when the Board next convenes in Detroit, Michigan, because of the fact that petitioners would be put to considerable expense in coming to Washington, D. C.

GODFREY HAMMEL,
PEARL HAMMEL,
Petitioners,
1248 Free Press Building, Detroit, Michigan.

5 [Duly sworn to by Godfrey Hammel and Pearl Hammel; jurats omitted in printing]

6 *Exhibit A to petition*

TREASURY DEPARTMENT,
Washington, May 13, 1936.

Mr. GODFREY HAMMEL and
Mrs. PEARL HAMMEL (Husband and Wife),
1248 Free Press Building, Detroit, Michigan.

SIR and MADAM: You are advised that the determination of your income tax liability for the taxable year(s) 1934 discloses a deficiency of $426.79 as shown in the statement attached.

In accordance with section 272 (a) of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully.

GUY T. HELVERING,
Commissioner.

By (Signed) CHAS T. RUSSELL,
Deputy Commissioner.

Enclosures:
Statement.
Form 870.

7 STATEMENT

IT:AR:D-1.
LB-90D.

In re: Mr. Godfrey Hammel and Mrs. Pearl Hammel (Husband and Wife), 1248 Free Press Building, Detroit, Michigan

INCOME TAX LIABILITY

Year, 1934; income tax liability, $1,555.44; income tax assessed, $1,128.65; deficiency, $426.79.

The deficiency shown herein is based upon the report dated January 18, 1936, prepared by Revenue Agent M. W. Fisher, a copy of which was transmitted to you.

Careful consideration has been accorded your protests dated February 29, 1936, and April 22, 1936, in connection with the findings of the examining officer.

Only $2,000.00 of the loss of $4,998.03 claimed on sale of farm by the sheriff due to the foreclosure of the mortgage is allowable as a deduction since it is held that the loss is a capital net loss from the sale of property. General Counsel's Memorandum 12737, Cumulative Bulletin XIII–1, page 120, appears to be applicable in this case.

Net income reported on return		$19,354.35
Add: Portion of loss claimed, disallowed		2,998.03
Corrected Net income		$22,352.38
Less: Personal exemption and credit for dependents		4,500.00
Net income subject to surtax		$17,852.38
Less:		
Dividends	$2,552.50	
Earned Income credit	1,007.87	3,560.37
Net income subject to normal tax		$14,292.01
Normal tax at 4% on $14,292.01		$571.68
Surtax on $17,852.38		983.76
Corrected income tax liability		$1,555.44
Income tax assessed, original, account No. 214056		1,128.65
Deficiency		$426.79

8 Before United States Board of Tax Appeals

Answer to motion of respondent and amendment to paragraph No. 7 of petitioners' statement of facts

Filed September 28, 1936

Petitioners make the following answer to Respondent's "Motion" filed September 15, 1936.

That one of the Petitioners, "Pearl Hammel," was adjudged bankrupt in the District Court of the United States, Eastern District of Michigan, on April 26, 1934, and she was duly discharged by this same Court on July 28, 1934.

Petitioners pray leave to amend Paragraph 7 of Petitioners' original statement of facts to read as follows:

"7—Petitioner, Pearl Hammel, was insolvent and in order to wipe out the deficiency judgment of $89,000.00 against her, she filed a petition in bankruptcy in the District Court of the United States, Eastern District of Michigan, on the 26th day of April, 1934, No. 17315, and was duly adjudged bankrupt." Further, on July 28, 1934, upon order of the District Court of the United States, Eastern District of Miehigan, she was duly discharged.

Petitioners respectfully pray that the Board will allow the amendment and deny the motion of Respondent.

Petitioners further state that no personal appearance will be made at the hearing of Respondent's motion.

GODFREY HAMMEL,
Petitioner.

PEARL HAMMEL,
Petitioner.

9 Before United States Board of Tax Appeals

Answer to petition and amendment to petition

Filed November 12, 1936

Comes now the Commissioner of Internal Revenue, by his attorney, Herman Oliphant, General Counsel for the Department of the Treasury, and for answer to the petition filed by the above-named petitioners, admits and denies as follows, to wit:

1, 2. Admits the allegations contained in Paragraphs 1 and 2 of the petition.

3. Admits that the taxes in controversy are income taxes for the calendar year 1934. Denies the remaining allegations contained in Paragraph 3 of the petition.

4 and 4 (a). Denies that the Commissioner erred as alleged in Paragraphs 4 and 4 (a) of the petition.

5, 6. Denies the allegations contained in Paragraphs 5 and 6 of the petition.

7. Denies the allegations contained in Paragraph 7 as amended by amendment filed on September 28, 1936.

8. Denies the allegations contained in Paragraph 8 of the petition.

Denies generally and specifically each and every allegation set forth in the petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the appeal be denied.

(Signed) HERMAN OLIPHANT,
General Counsel,
For the Department of the Treasury.

Of Counsel:
CHESTER A. GWINN,
HUGH R. DOWLING,
Special Attorneys,
Bureau of Internal Revenue.

10 Before United States Board of Tax Appeals

Memorandum opinion

Entered December 30, 1937

VAN FOSSAN: Respondent determined a deficiency of $426.79 in income tax of petitioner for the year 1934 consequent on his conclusion that a certain loss deducted by petitioner was a capital net loss and not an ordinary loss. The facts were stipulated substantially as follows:

During the years 1926 to 1930, both inclusive, the petitioner Pearl Hammel invested the sum of $4,998.03 in a speculative land syndicate, which syndicate purchased on land contract 80 acres of land in Oakland County, Michigan, known as "The Adams Farm," the purchase price being $96,000. The syndicate made a down payment of $20,000,

and thereafter approximately $4,000 additional was paid on the principal, leaving an unpaid balance of approximately $72,000, plus accrued interest and State and County taxes for several years.

One Charles L. Bruce acted as Trustee for the purchasers (the syndicate members).

Because of the general financial condition of the country, the value of the land, and other lands in Oakland County, Michigan. depreciated to the extent that the land referred to decreased in value to the value of farm land and was worth, in 1934, approximately $8,000.

The petitioner, Pearl Hammel, and other members of the syndicate, were unable to meet the payments called for by the contract and were in default, and the seller on the contract, Mrs. Julia Adams, commenced foreclosure proceedings in Chancery in the Oakland County Circuit Court and obtained a decree of foreclosure without any equity of redemption, which decree was affirmed by a decision of the Michigan Supreme Court and a decree entered thereon in the year 1934, pursuant to which decree the property was sold on March 26, 1934, by the sheriff and the sheriff's deed issued to Mrs. Julia Adams. Julia Adams, in the Supreme Court proceedings, obtained a deficiency judgment against all of the members of the syndicate, jointly and severally, in the amount of approximately $79,000. The petitioner, Pearl Hammel, was insolvent, and in order to be relieved of the deficiency judgment of approximately $79,000, filed a voluntary petition in bankruptcy in the District Court of the United States for the Eastern District of Michigan, Southern Division, on April 26, 1934, and was duly discharged in bankruptcy on July 28, 1934.

11 The sole asset of the syndicate was the property herein referred to, and the syndicate had no assets whatsoever left to distribute among its members.

The sole issue is agreed to be whether the loss in the sum of $4,998.03 is a loss resulting from the "sale or exchange" of the property, and, therefore, within the purview of section 117 (d) of the Revenue Act of 1934:

Limitation on Capital Losses.—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. * * *

or whether the loss is an ordinary loss allowable as a deduction in full under and within the purview of section 23 (e) (2) of the Revenue Act of 1934:

Losses by Individuals.—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

* * * * * * *

(2) if incurred in any transaction entered into for profit; though not connected with the trade or business; * * *

Addressing ourselves to the issue before us, i. e., the interpretation of section 117 (d), our observation in John H. Watson, Jr.,

27 B. T. A. 463, is precisely pertinent. There we said, "The words 'sale or exchange' are ordinary words of well established meaning." It is fundamental that the language of the revenue act is to be taken in its ordinary meaning. Hale v. Helvering, 85 Fed. (2d) 819. Here there is nothing in the context to indicate an intention to give the words "sale or exchange" an exotic meaning.

Thus the problem becomes one of application. Under the above facts, was the loss sustained on a sale or exchange of property? Giving the words "sale or exchange" their ordinary meaning, we are of the opinion the loss did not arise from a transaction properly to be so characterized. Petitioner neither sold nor exchanged anything. She lost her property through the operation of the law of foreclosure. The sale by the sheriff effected a transfer of title to the property but it did not constitute a sale or exchange by taxpayer. The purchaser at the foreclosure sale got a sheriff's deed, not a deed from the petitioner.

12 Thus it is that we are unable to find any justification for respondent's holding that the loss arose from a sale or exchange.

On the other hand, we believe the loss is properly to be placed under section 23 (e) (2). This section is broad in scope. Petitioner entered into a transaction for profit when she bought the property. The transaction was closed and the loss sustained when the property was taken from her by foreclosure.

It follows that petitioner's loss is not to be limited by the provisions of section 117 (d).

Judgment will be entered for the petitioner.

[SEAL]

Before United States Board of Tax Appeals

Decision

Entered December 31, 1937

Pursuant to the determination of the Board, as set forth in its Memorandum Opinion, entered December 30, 1937, it is

Ordered and decided: That there is no deficiency in income tax for the year 1934.

[SEAL] (Signed) ERNEST H. VAN FOSSAN,
Member.

13 Before United States Board of Tax Appeals

Petition for review and assignments of error

Filed March 24, 1938

To the Honorable Judges of the United States Circuit Court of Appeals for the Sixth Circuit:

Now comes Guy T. Helvering, Commissioner of Internal Revenue, by his attorneys, James W. Morris, Assistant Attorney General,

J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and Harold F. Noneman, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

I

That he is the duly appointed, qualified, and acting Commissioner of Internal Revenue, appointed and holding office by virtue of the laws of the United States; that Godfrey and Pearl Hammel are individuals and are husband and wife, residing together; that the respondents executed a joint Federal income-tax return for the calendar year 1934 and filed the same with the Collector of Internal Revenue for the District of Michigan, whose office is located at Detroit, Michigan, which is within the jurisdiction of this honorable court.

That the court in which the review of this proceeding is sought is the United States Circuit Court of Appeals for the Sixth Circuit.

II

The nature of the controversy is as follows, to wit:

During the years 1926 to 1930, both inclusive, the petitioner Pearl Hammel invested the sum of $4,998.03 in a speculative land syndicate, which syndicate purchased on land contract 80 acres of land in Oakland County, Michigan, known as "The Adams Farm," the purchase price being $96,000. The syndicate made a down payment of $20,000, and thereafter approximately $4,000 additional was paid on the principal, leaving an unpaid balance of approximately $72,000, plus accrued interest and State and County taxes for several years.

One Charles L. Bruce acted as Trustee for the purchasers (the syndicate members).

Because of the general financial condition of the country, the value of the land, and other lands in Oakland County, Michi-
14 gan, depreciated to the extent that the land referred to decreased in value to the value of farm land and was worth, in 1934, approximately $8,000.

The petitioner Pearl Hammel and other members of the syndicate were unable to meet the payments called for by the contract and were in default and the seller on the contract, Mrs. Julia Adams, commenced foreclosure proceedings in Chancery in the Oakland County Circuit Court and obtained a decree of foreclosure without any equity of redemption, which decree was affirmed by a decision of the Michigan Supreme Court and a decree entered thereon in the year 1934, pursuant to which decree the property was sold on March 26, 1934, by the sheriff and the sheriff's deed issued to Mrs. Julia Adams. Julia Adams, in the Supreme Court proceedings, obtained a deficiency judgment against all of the members of the syndicate, jointly and severally, in the amount of approximately $79,000. The petitioner, Pearl Hammel, was insolvent, and in order to be relieved

of the deficiency judgment of approximately $79,000, filed a voluntary petition in bankruptcy in the District Court of the United States for the Eastern District of Michigan, Southern Division, on April 26, 1934, and was duly discharged in bankruptcy on July 28, 1934.

The sole asset of the syndicate was the property herein referred to, and the syndicate had no assets whatsoever left to distribute among its members.

As a result the respondent, Pearl Hammel, sustained a loss of $4,998.03. The respondents filed a joint Federal income-tax return for the calendar year 1934 in which this amount was deducted in arriving at the taxable net income.

On May 13, 1936, the Commissioner mailed to the respondents aforesaid a notice of deficiency in Federal income tax for the calendar year in the amount of $426.79. In determining the deficiency in the tax the Commissioner limited the deduction in connection with the aforesaid loss to $2,000.00, pursuant to the provisions of Section 117 (d) of the Revenue Act of 1934 (48 Stat. 714, U. S. C. Title 26, Sec. 101), as a loss sustained from the sale or exchange of a capital asset.

On August 10, 1936, the respondents on review filed an appeal with the United States Board of Tax Appeals from the Commissioner's determination of the deficiency as set forth in the notice of deficiency aforesaid. After the answer of the Commissioner was duly
15 filed, the case was submitted to the Board of Tax Appeals for decision upon the pleadings and a stipulation of facts. The opinion and interlocutory decision of the Board of Tax Appeals was entered December 30, 1937, and the final order of the Board redetermining the deficiency was entered December 31, 1937, in which it was ordered and decided that there was no deficiency in income tax due from the respondents for the calendar year 1934.

III

The Commissioner of Internal Revenue, being aggrieved by the conclusions of law contained in the decision of the Board of Tax Appeals, and by its order redetermining the deficiency in the tax, desires to obtain a review thereof by the United States Circuit Court of Appeals for the Sixth Circuit.

The Commissioner's assignments of error are as follows:

(1) The Board of Tax Appeals erred in that its decision is not supported by and is contrary to the evidence.

(2) The Board of Tax Appeals erred in holding and deciding that the petitioner, Pearl Hammel, sustained an ordinary loss upon the disposition of property instead of holding and deciding that she sustained a capital loss upon the sale or exchange of a capital asset.

(3) The Board of Tax Appeals erred in not holding and deciding that the petitioner, Pearl Hammel, sustained a capital loss upon the

sale or exchange of a capital asset, instead of holding and deciding that she sustained an ordinary loss upon the disposition of property.

(4) The Board of Tax Appeals erred in entering its final order of redetermination that there is no deficiency in the income tax of the petitioners for the year 1934 instead of a deficiency of $426.79, as determined by the Commissioner.

(5) The Board of Tax Appeals erred in failing and refusing to enter a final order of redetermination that there is due from the petitioners a deficiency in income tax for the year 1934 in the amount of $426.79, instead of no deficiency.

Wherefore, the Commissioner petitions that the decision of
16 the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Sixth Circuit, that a transcript of the record be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing, and that appropriate action be taken to the end that the errors complained of may be reviewed and corrected by said court.

(Signed) JAMES W. MORRIS,
Assistant Attorney General.

(Signed) J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:
HAROLD F. NONEMAN,
Special Attorney,
Bureau of Internal Revenue.

[*Duly sworn to by Harold F. Noneman; jurat omitted in printing.*]

17 Before United States Board of Tax Appeals

Notice of filing petition for review

Filed April 4, 1938

To GODFREY HAMMEL and PEARL HAMMEL,
1248 Free Press Building, Detroit, Michigan.

You are hereby notified that the Commissioner of Internal Revenue did, on the 24th day of March 1938 file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Sixth Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 24th day of March 1938.

(Signed) J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 29th day of March 1938.

(Signed) GODFREY HAMMEL,
(Signed) PEARL HAMMEL,
Respondents on Review.

18 Before United States Board of Tax Appeals

Notice of filing petition for review

Filed April 4, 1938

To JOHN J. SLOAN, *Esq.*,
Dime Bank Building, Detroit, Michigan.

You are hereby notified that the Commissioner of Internal Revenue did, on the 24th day of March 1938 file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Sixth Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 24th day of March 1938.

(Signed) J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 30th day of March 1938.

(Signed) JOHN J. SLOAN,
Counsel for Respondents on Review.

19 Before United States Board of Tax Appeals

Stipulation of facts

Filed July 6, 1937

It is hereby stipulated by and between the parties to the above-entitled cause, through their respective counsel, as follows:

I

That during the years 1926 to 1930, both inclusive, the petitioner, Pearl Hammel, invested the sum of Four Thousand Nine Hundred Ninety-Eight and 03/100 Dollars ($4,998.03) in a speculative land syndicate, which syndicate purchased on land contract eighty (80) acres of land in Oakland County, Michigan, known as "The Adams Farm," the purchase price being Ninety-Six Thousand Dollars ($96,000.00).

II

That said syndicate made a down payment of Twenty Thousand Dollars ($20,000.00) and thereafter approximately Four Thousand Dollars ($4,000.00) additional was paid on the principal, leaving an unpaid balance of approximately Seventy-Two Thousand Dollars ($72,000.00), plus accrued interest and State and County taxes for several years.

III

That one Charles L. Bruce acted as Trustee for the Purchasers (the Syndicate members).

IV

That because of the general financial condition of the country, the value of said land, and other lands in Oakland County, Michigan, depreciated to the extent that the land referred to decreased in value to the value of farm land and was worth, in 1934, approximately Eight Thousand Dollars ($8,000.00).

V

That the petitioner, Pearl Hammel, and other members of the Syndicate, were unable to meet the payments called for by the contract and were in default, and the Seller on said contract, Mrs. Julia Adams, commenced foreclosure proceedings in Chancery in the Oakland County Circuit Court and obtained a decree of foreclosure without any equity of redemption, which decree was affirmed by a decision of the Michigan Supreme Court and a decree entered thereon in the year 1934, pursuant to which decree the property was sold on March 26, 1934, by the sheriff and the Sheriff's deed issued to the said Mrs. Julia Adams; that the said Julia Adams in said Supreme Court proceedings obtained a deficiency judgment against all of the members of the Syndicate, jointly and severally, in the amount of approximately Seventy-Nine Thousand Dollars ($79,000.00). The petitioner, Pearl Hammel, was insolvent, and in order to be relieved of said deficiency judgment of approximately Seventy-Nine Thousand Dollars ($79,000.00), filed a voluntary petition in bankruptcy in the District Court of the United States for the Eastern District of Michigan, Southern Division, on, to-wit: the 26th day of April, 1934, and was duly discharged in bankruptcy on, to-wit: July 28, 1934.

VI

That the sole asset of said Syndicate was the property herein referred to, and that said Syndicate had no assets whatsoever left to distribute among its members.

VII

It is further stipulated and agreed, the facts herein being agreed upon, so far as legally permissible for the parties to do, that the sole issue is whether the loss of the said Pearl Hammel in the sum of Four Thousand Nine Hundred Ninety-Eight and 03/100 Dollars ($4,998.03) is a loss resulting from the "sale or exchange" of said property, and therefore within the purview of Section 117–D of the Revenue Act of 1934, or whether said loss is an ordinary loss allowable as a deduction in full under and within the purview of Section 23–E2 of the Revenue Act of 1934.

(Signed) JOHN J. SLOAN,
Attorney for Petitioners.
(Signed) MORRISON SHAFROTH,
Attorney for Respondent.

JOHN J. SLOAN,
Attorney for Petitioners,
1020 Dime Bank Building, Detroit, Michigan.

Dated: June —, 1937.

21 Before United States Board of Tax Appeals

Praecipe for record

Filed June 10, 1938

To the CLERK OF THE UNITED STATES BOARD OF TAX APPEALS:

You will please prepare, transmit, and deliver to the Clerk of the United States Circuit Court of Appeals for the Sixth Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Sixth Circuit, heretofore filed by the Commissioner of Internal Revenue.

1. Docket entries of the proceedings before the Board.
2. The following pleadings before the Board:
(a) Petition, including the copy of the notice of deficiency annexed thereto as "Exhibit A."
(b) Answer.
3. Opinion and decision of the Board.
4. Petition for review, together with proof of service of notices of filing petition for review and of service of copies of petition for review.
5. Stipulation of facts filed by the parties at the hearing on July 6, 1937.
6. This praecipe.

(Signed) J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue.

Service of a copy of the within praecipe is hereby admitted this 7th day of June 1938.

(Signed) JOHN J. SLOAN,
Attorney for Respondents.

22 [Clerk's certificate to foregoing transcript omitted in printing.]

Before United States Board of Tax Appeals

Order enlarging time

On motion of counsel for the petitioner, it is

Ordered: That the time for preparation of the evidence and transmission and delivery of the record sur petition for review of the above-entitled proceeding in the United States Circuit Court of Appeals for the Sixth Circuit, be and it is hereby extended to June 22, 1938.

(S) C. R. ARUNDELL, *Member.*

Dated Washington, D. C., May 17, 1938.

Now, June 18, 1937, the foregoing order enlarging time certified from the record as a true copy.

[SEAL]

B. D. GAMBLE, *Clerk,*
U. S. Board of Tax Appeals.

23 In United States Circuit Court of Appeals for the Sixth Circuit

Minute entry of argument and submission

December 13, 1939

Before HICKS, HAMILTON, and ARANT, JJ.

This cause is argued by A. A. Armstrong for Petitioner and by John J. Sloan for Respondents and is submitted to the court.

In United States Circuit Court of Appeals

Decree

Entered January 10, 1940

Appeal from the United States Board of Tax Appeals.

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the order or decree of the said Board of Tax Appeals in this cause be and the same is hereby affirmed.

24 [File endorsement omitted.]

In United States Circuit Court of Appeals, Sixth Circuit

No. 8043

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

GODFREY HAMMEL and PEARL HAMMEL, RESPONDENTS

On petition for Review of Decision of the United States Board of Tax Appeals

Opinion

Filed January 10, 1940

Before HICKS, HAMILTON, and ARANT, Circuit Judges.

HAMILTON, Circuit Judge. This is a petition by the Commissioner of Internal Revenue to review a decision of the Board of Tax Appeals disallowing a deficiency in income taxes of $426.00 for the calendar year 1934, found by him to be due from the respondents, but disallowed by the Board.

The statutes involved are Sections 23 (e) (2) (Title 26 U. S. C. A., Sec. 23), Section 111 (a) Title 26 (U. S. C. A., Sec. 111), Section 117 (a) (b) (d) (Title 26 U. S. C. A., Sec. 101).

During the years 1926 to 1930, both inclusive, the respondents, Godfrey Hammel and Pearl Hammel, husband and wife, paid $4,998.03 into a syndicate of which they were members on a land contract which it had purchased, consisting of 80 acres of land in Oakland County, Michigan. The purchase price was $96,000.00 and the syndicate paid $20,000.00 at the time of pu'chase and thereafter approximately $4,000.00, leaving unpaid $72,000.00 together with accrued interest and delinquent state and county taxes.

In 1934, the property, being worth no more than approximately $8,000.00 and the syndicate having defaulted in payments, the
25 vendor, Julia Adams, commenced foreclosure proceedings in the Oakland County Circuit Court and obtained a foreclosure decree without equity of redemption which on appeal the Michigan Supreme Court affirmed and on March 26, 1934, the Sheriff, pursuant to said decree, sold the property at public auction which resulted in a deficiency judgment of approximately $79,000.00 against the syndicate members jointly and severally.

On April 26, 1934, the respondent, Pearl Hammel, was adjudged a bankrupt and discharged July 28, 1934. The land was the sole asset of the syndicate and none of its members received any sum in distribution. The respondents lost the entire $4,998.03, which they had paid in and filed a joint income tax return for the calendar year 1934, deducting this sum as a loss. The petitioner on audit and

review reduced the loss to $2,000.00 pursuant to the provisions of Section 117 (d) of the Revenue Act of 1934 (48 Stat. 714, U. S. C. A. 26, Sec. 101).

Respondents appealed to the Board of Tax Appeals from the deficiency, which decided that the entire loss was deductible under the provisions of Section 23 (e) (2) of the Revenue Act of 1934 (48 Stat. 680, U. S. C. A. 26, Sec. 23), hence this appeal.

The Revenue Act of 1934 (c. 227, 48 Stat. 680) provides that in computing the taxable net income of an individual for the taxable year there may be deducted from gross income losses sustained during the year from any transaction entered into for profit [Sec. 23 (e) (2)]. The deductible loss from the "sale" or other disposition of property is determined by subtracting the amount realized from the cost basis, less depreciation, plus capital expenditures, etc. [Sec. 111 (a)] but if the loss results from the "sale or exchange" of a "capital asset" [Sec. 117 (b)] only a specified percentage of the loss realized may be deducted in determining net income [Sec. 117 (a)] and the total deduction may not exceed $2,000.00 plus gains from sales or exchanges of capital assets [Sec. 117 (d)].

In the case at bar the parties have stipulated that respondents lost $4,998.03 during the taxable year and it is conceded that this loss is deductible unless limited to $2,000.00 under Section 117 (d). It is also conceded that the interest involved was a capital asset and the loss determinable at the time of the foreclosure sale. The question thus narrows itself to the simple one as to whether a foreclosure by a vendor is a sale, as that word is used in the Revenue Act.

It is unquestionably within the competence of the Congress
26 when imposing a tax to modify or abrogate for the purpose of the Act any rule of law or equity which otherwise would be applicable to the subject matter. Whether it has done so or not must always be a question of the true construction of the particular statute under consideration and the only method of interpretation is to ascertain the intention of the Congress from the language and provisions of the Act itself, and it is presumed that the words used therein are to be given their known and ordinary signification. Their popular import furnishes the general rule for interpretation and their plain, obvious, and rational meaning is always preferred to any curious, narrow, or hidden sense. Old Colony Railroad Company v. Commissioner, 284 U. S. 552, 560.

Under the laws of Michigan, when a vendee defaults on a land contract containing the usual forfeiture clause, the vendor may treat it as continuing in force and sue at law for payments due or bring suit in equity for a foreclosure of his lien or he may declare the contract forfeited. On a declaration of forfeiture, the contract is ended and the vendor is relieved of the duty to convey and the vendee of the duty to pay. On an equitable foreclosure, the vendor may obtain a deficiency judgment. Chicago Boulevard Land Company v. Apartment Garages, 245 Mich. 448; Bernard v. Huff, 252 Mich. 258.

It follows that the vendor here in question had the right to deprive the respondents and their joint adventurers of all interest in the property by a declaration of forfeiture and the only additional advantage of foreclosure was to obtain a deficiency judgment.

"Sale" is a word of precise legal import. Its elements are (1) parties competent to contract, (2) mutual consent, (3) a thing the absolute or general property in which is transferred from the seller to the buyer, (4) a price in money paid or promised. Butler v. Thomson, 92 U. S. 412, 414; Williamson v. Berry, 49 U. S. 495, 544. There is nothing in the legislative history of the statute in question or in the language of the act indicating that the Congress used the word "sale" in any sense other than its precise legal import or plain and obvious meaning.

If any one of the above elements be absent, it is not a sale as that word is understood in its ordinary signification.

The respondents in the case at bar were not parties to the sheriff's sale and neither contracted for nor consented to it and received no part of the consideration. They were deprived of their interest in the property not by sale but by an adverse judicial proceeding which completely extinguished their title without consideration.

27 The foreclosure was the identifiable event which established their loss. However, it was not established by a sale as that word is used in Section 117 of the Revenue Act of 1934. Commissioner of Internal Revenue v. Triehofer, 102 F. (2d) 787 (C. C. A. 3); Burnet v. Harmel, 287 U. S. 103, 107; Hale v. Helvering, 85 F. (2d) 819 (C. C. A. D. C.).

The order of the Board is affirmed.

28 [Clerk's certificate to foregoing transcript omitted in printing.]

29 Supreme Court of the United States

Order allowing certiorari

Filed May 20, 1940

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Sixth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsement on cover:] File No. 44302. U. S. Circuit Court of Appeals, Sixth Circuit. Term No. 49. Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, vs. Godfrey Hammel and Pearl Hammel. Petition for a writ of certiorari and exhibit thereto. [Filed April 10, 1940. Term No. 49 O. T. 1940.]

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In the Supreme Court of the United States

OCTOBER TERM, 1939

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

GODFREY HAMMEL AND PEARL HAMMEL

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Sixth Circuit entered in the above-entitled cause on January 10, 1940.

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 10) is unreported. The opinion of the Circuit Court of Appeals is reported in 108 F. (2d) 753.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on January 10, 1940. The jurisdiction

of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a foreclosure sale constitutes a "sale" within the meaning of Sections 23 (j) and 117 (d) of the Revenue Act of 1934, limiting the deduction of capital losses.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME.
>
> In computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (j) CAPITAL LOSSES.—Losses from sales or exchanges of capital assets shall be allowed only to the extent provided in section 117 (d).
>
> * * * * *
>
> [U. S. C., Title 26, Sec. 23.]
>
> SEC 117. CAPITAL GAINS AND LOSSES.
>
> * * * * *
>
> (d) LIMITATION ON CAPITAL LOSSES.—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. * * *
>
> * * * * *
>
> [U. S. C., Title 26, Sec. 101.]

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 117–2. *Limitations on capital gains and capital losses.*— * * *

Section 117 (d) provides a limitation on deductions for capital losses affecting all taxpayers including corporations, that is, losses from sales or exchanges of capital assets shall be allowed as deductions only to the extent of $2,000 plus the gains from such sales and exchanges. * * *

STATEMENT

The facts, as found by the Board of Tax Appeals (R. 10–11), are substantially as follows:

During the years 1926 to 1930, both inclusive, the taxpayer, Pearl Hammel, invested $4,998.03 in a speculative land syndicate, which syndicate purchased on land contract 80 acres of land in Oakland County, Michigan, known as "The Adams Farm", the purchase price being $96,000. The syndicate made a down payment of $20,000, and thereafter approximately $4,000 additional was paid on the principal, leaving an unpaid balance of approximately $72,000, plus accrued interest and state and county taxes for several years. (R. 10.)

One Charles L. Bruce acted as trustee for the purchasers (the syndicate members). (R. 10.)

Because of the general financial condition of the country, the value of the land, and other lands in Oakland County, Michigan, depreciated; by 1934 the land referred to had decreased in value to the value of farm land and was worth approximately $8,000. (R. 10.)

The taxpayer, Pearl Hammel, and other members of the syndicate, were unable to meet the payments called for by the contract and were in default, whereupon the vendor, Mrs. Julia Adams, commenced foreclosure proceedings in Chancery in the Oakland County Circuit Court and obtained a decree of foreclosure without any equity of redemption. The decree was affirmed by a decision of the Michigan Supreme Court in 1934, pursuant to which the property was sold on March 26, 1934, by sheriff's deed to Mrs. Adams. Mrs. Adams also obtained a deficiency judgment against all of the members of the syndicate, jointly and severally, in the amount of approximately $79,000. The taxpayer, Pearl Hammel, was insolvent, and in order to be relieved of the deficiency judgment, filed a voluntary petition in bankruptcy in the District Court of the United States for the Eastern District of Michigan, Southern Division, on April 26, 1934, and was duly discharged in bankruptcy on July 28, 1934. (R. 10.)

The sole asset of the syndicate was the property herein referred to. (R. 11.)

The respondents are husband and wife, living together, and filed a joint income tax return for the taxable year 1934 in which they claimed a loss deduction of $4,998.03. The Commissioner held that the loss was a capital net loss, and accordingly disallowed all but $2,000 of the deduction claimed, in accordance with Section 117 (d) of the Revenue Act of 1934, *supra*. (R. 3, 7.)

The Board of Tax Appeals held that the loss sustained did not result from a "sale" or "exchange," and was therefore not subject to the limitation prescribed for capital losses. The court below affirmed.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the foreclosure sale was not a "sale" within the meaning of Sections 23 (j) and 117 (d) of the Revenue Act of 1934.

2. In failing to hold that the loss sustained by the taxpayer upon the foreclosure sale was subject to the limitation prescribed by Sections 23 (j) and 117 (d) of the Revenue Act of 1934.

3. In affirming the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

The Circuit Court of Appeals held that a foreclosure sale was not a "sale" within the meaning of Section 117 (d) of the Revenue Act of 1934, *supra,* limiting the loss deduction allowed upon sales or exchanges of capital assets, and accordingly allowed the deduction in full. The decision below is in direct conflict with *Commissioner* v. *Electro-Chemical Engraving Co.* (C. C. A. 2d), decided March 18, 1940, not yet officially reported, but may be found in 1940 Prentice-Hall, Vol. 4, p. 62,634.[1] In that case, in holding that a foreclosure

[1] The *Electro Chemical* case involved a foreclosure sale under a purchase money mortgage while in the instant case

sale constituted a sale within the meaning of Section 117 (d) of the Revenue Act of 1934, the Circuit Court of Appeals for the Second Circuit recognized that its decision was in conflict with the decision below and with *Commissioner* v. *Freihofer*, 102 F. (2d) 787 (C. C. A. 3d), upon which the court below relied, and stated that "We feel compelled to differ with the foregoing decisions".

The question presented by the instant case is of considerable importance in the administration of the revenue laws. Similar questions are involved in five cases now pending before the Circuit Courts of Appeals.[2]

CONCLUSION

Wherefore it is respectfully submitted that this petition should be granted.

FRANCIS BIDDLE,
Solicitor General.

APRIL, 1940.

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a land purchase contract was foreclosed. However, that distinction appears to be entirely immaterial.

[2] *Bookstein* v. *Commissioner* (B. T. A. unreported opinion of September 23, 1939), now pending in the Circuit Court of Appeals for the Sixth Circuit; *Nebraska Bridge Supply & Lumber Co.* v. *Commissioner*, 40 B. T. A. 40, now pending in the Circuit Court of Appeals for the Eighth Circuit; *Jones* v. *Commissioner* (B. T. A. unreported opinion of September 30, 1939), now pending in the Circuit Court of Appeals for the Eighth Circuit); *Coggan* v. *Commissioner* (B. T. A. unreported opinion of October 27, 1939), now pending in the Circuit Court of Appeals for the First Circuit; *Hill* v. *Commissioner*, 40 B. T. A. 376, now pending in the Circuit Court of Appeals for the Sixth Circuit.

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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 49

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

GODFREY HAMMEL AND PEARL HAMMEL

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 6–8) is unreported. The opinion of the Circuit Court of Appeals (R. 16–18) is reported in 108 F. (2d) 753.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 10, 1940 (R. 15). Petition for certiorari was filed April 10, 1940, and granted May 20, 1940 (R. 18). The jurisdiction of this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The taxpayer purchased an interest in real estate. Upon default under the purchase contract the property was sold at foreclosure. The question presented is whether the resulting loss was a capital loss subject to the limitations on deductibility contained in Section 117 of the Revenue Act of 1934. The answer to this question depends upon whether the foreclosure sale constituted a "sale" or "exchange" within the meaning of Section 117 (d).

STATUTE INVOLVED

The statute involved is set out in Appendix A, *infra.*

STATEMENT

The facts, as stipulated (R. 12–14), may be summarized as follows:

In 1926 taxpayer Pearl Hammel [1] and others as members of a syndicate purchased "on land contract" 80 acres of land in Oakland County, Michigan, for $96,000, $20,000 of which was paid down. Thereafter, additional payments amounting to $4,000 were made. The taxpayer contributed $4,998.03 of the total cash payments of $24,000. (R. 12–13.)

By 1934 the value of this property had decreased to approximately $8,000 and the taxpayer and her

[1] The taxpayer Pearl Hammel and her husband, Godfrey Hammel, filed a joint return (R. 2) and both are parties to this proceeding. The word taxpayer as hereinafter used in this brief refers to Pearl Hammel.

associates were unable to meet the payments called for by the contract. The vendor instituted foreclosure proceedings in the Circuit Court of Oakland County, Michigan, and obtained a decree of foreclosure "without any equity of redemption", which was affirmed by the Michigan Supreme Court and pursuant to which the property was sold on March 26, 1934. At the sale, which was conducted by the sheriff, Mrs. Adams, the land contract vendor, bought in the property and received the sheriff's deed. (R. 13.)

The vendor obtained a deficiency judgment in the Supreme Court proceedings against the members of the syndicate jointly and severally in the amount of approximately $79,000. The principal balance due was $72,000. Taxpayer thereupon on April 26, 1934, filed a petition in bankruptcy and was duly discharged on July 28, 1934. (R. 13.)

It is stipulated that the sole issue is whether taxpayer's loss of $4,998.03 resulted from the "sale or exchange" of the mentioned property and therefore was within the purview of Section 117 (d) of the Revenue Act of 1934, or whether it was an ordinary loss deductible in full under Section 23 (e) (2) of that Act. (R. 14.) The Board of Tax Appeals upheld the taxpayer's contention that Section 117 of the 1934 Act was not applicable. Its decision was affirmed by the Circuit Court of Appeals.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the foreclosure sale was not a "sale" within the meaning of Sections 23 (j) and 117 (d) of the Revenue Act of 1934.

2. In failing to hold that the loss sustained by the taxpayer upon the foreclosure sale was subject to the limitation prescribed by Sections 23 (j) and 117 (d) of the Revenue Act of 1934.

3. In affirming the decision of the Board of Tax Appeals.

SUMMARY OF ARGUMENT

The sole question presented is whether the taxpayer's loss resulted from a "sale or exchange" of a capital asset within the meaning of Sections 23 (j) and 117 of the Revenue Act of 1934. If it did, her deductible loss is limited by Section 117 (d) to her capital gains plus $2,000.

The taxpayer has failed to show that the vendor under the land contract retained the title to the property. But even if title was retained, the beneficial ownership passed to the taxpayer and her associates. This beneficial ownership was a capital asset within the meaning of Section 117 (d) of the Act. The foreclosure sale was a "sale" according to one of the ordinary and accepted meanings of the term and transferred the beneficial ownership of the taxpayer and her associates to the purchaser. Their interest was not extinguished by the foreclosure proceedings but was transferred by the sale.

The foreclosure sale fixed the price which the property brought and this price represented the consideration received by the taxpayer and her associates since it was applied in reduction of their indebtedness to the vendor under the sales contract. The situation is substantially the same as one in which a mortgagor transfers property to a mortgagee in partial or full satisfaction of the mortgage debt. Such transactions have been consistently held to constitute sales within the meaning of the statute involved.

The fact that the taxpayer was not a party to and did not consent to the foreclosure sale furnishes no basis for holding that this case is not governed by Section 117 (d). Since the statutory words include involuntary as well as voluntary sales and a deduction from income is involved, clear evidence of the legislative intent would be required to justify a reformation of the statute. The legislative history prior to 1934 discloses no intention to limit the capital loss provisions to voluntary sales. The reasons underlying the enactment of Section 117 of the Revenue Act of 1934, which fundamentally changed the treatment of capital gains and losses, show a definite intent to include involuntary transactions, since a primary purpose was to achieve greater stability in the revenues and to lessen the effect of capital losses on ordinary income.

Congress has indicated an intention to enlarge rather than restrict the scope of the phrase "sales or exchanges" by including transactions, many of which are involuntary, and which, although not sales or exchanges, are similar in result. In the Revenue Act of 1938, capital loss provisions are made applicable to losses from worthless securities, which are purely involuntary in character. If Congress had thought that the phrase "sales or exchanges" as theretofore used had included only voluntary transactions, it probably would have expressly broadened the scope of the phrase as used in Section 117 of the 1938 Act, which it did not do. An interpretation limiting the capital loss provisions to voluntary sales would result in doubts as to the application of the statute and administrative difficulties which Congress cannot be presumed to have intended.

ARGUMENT

THE TAXPAYER'S LOSS RESULTED FROM THE "SALE" OF A CAPITAL ASSET

1. The taxpayer Pearl Hammel claimed, and the Board and Circuit Court of Appeals for the Sixth Circuit allowed her, a deduction for loss incurred in a transaction entered into for profit. Revenue Act of 1934, Section 23 (e) (2), Appendix A, *infra*. The Commissioner unsuccessfully contended that her loss resulted from a "sale or exchange" of a capital asset, within the meaning of Sections 23 (j) and 117 of that Act, Appendix, *infra*. Whether

it did, and, in particular, whether the taxpayer's deductible loss is limited to $2,000, as provided in Section 117 (d), is the sole issue to be decided by this Court.

The transaction for profit was the purchase by the taxpayer and her associates of Michigan real estate pursuant to the terms of what is referred to in the stipulation as a "land contract." The taxpayer has assumed in her argument below that title was at all times retained by the vendor under the contract, an unwarranted assumption in the absence of the contract itself, which the taxpayer, who bore the burden of proof, has not introduced into the record. But even if the assumption is permissible, it is obvious that the vendor was not the true owner of the property but retained a security title only. *Bowen* v. *Lansing,* 129 Mich. 117, 120, 88 N. W. 384. Beneficial ownership, including the right to possession and the rents and profits and the power to transfer those rights to others, quite obviously passed to the taxpayer and her associates by reason of the contract. *Fitzhugh* v. *Maxwell,* 34 Mich. 138; *Walker* v. *Casgrain,* 101 Mich. 604, 60 N. W. 291.[2] Such ownership was in these re-

[2] In *Walker* v. *Casgrain,* 101 Mich. 604, the court said (p. 608): "While * * * [the vendor] holds the legal title * * * [the vendee] is the owner in equity. The claim of the vendor is but an ordinary money debt, secured by the contract." The last sentence was quoted with approval in *Lutz* v. *Dutmer,* 286 Mich. 467, 482, 282 N. W. 431, 436. In equity the interest of the vendee is treated as

spects like that of a mortgagor. Cf. *Barnard* v. *Huff*, 252 Mich. 258, 261, 233 N. W. 213, 214. It could not be and has not been disputed that the beneficial ownership held and lost by the taxpayer and her associates was a "capital asset" within the meaning of Section 117 (b) of the 1934 Act, Appendix, *infra*. The question is thus whether their loss resulted "from" the "sale or exchange" of that asset within the meaning of Section 117 (d). In holding that it did not, the decision of the Circuit Court of Appeals in this case follows *Commissioner* v. *Freihofer*, 102 F. (2d) 787 (C. C. A. 3d), but is in conflict with *Commissioner* v. *Electro-Chemical E. Co.*, 110 F. (2d) 614 (C. C. A. 2d), pending on certiorari, No. 62, present Term.

The decision of the court below that the taxpayer's loss did not result from a sale within the meaning of the statute apparently is rested on grounds which are summarized in the following excerpt from the opinion (R. 18):

> The respondents in the case at bar were not parties to the sheriff's sale and neither contracted for nor consented to it and re-

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realty. *Bowen* v. *Lansing*, *supra*; *Starkweather* v. *Chatfield*, 149 Mich. 443, 112 N. W. 1071; *Comfort* v. *Robinson*, 155 Mich. 143, 150, 118 N. W. 943. The interest of the vendor is a chose in action which becomes part of his personalty. *Detroit Trust Co.* v. *Baker*, 230 Mich. 551, 203 N. W. 154; *Bowen* v. *Lansing*, *supra*. Cf. *City of Marquette* v. *Iron & Land Co.*, 132 Mich. 130, 92 N. W. 934. The rule of equitable conversion is not followed under all circumstances. *Union Guardian Trust Co.* v. *Rood*, 261 Mich. 188, 246 N. W. 74; 265 Mich. 354, 251 N. W. 309.

> ceived no part of the consideration. They were deprived of their interest in the property not by sale but by an adverse judicial proceeding which completely extinguished their title without consideration.

We submit that the interpretation adopted by the court is contrary to the plain terms of the statute and the legislative purpose in enacting it.[3]

2. It is clear that the foreclosure sale was a "sale." Webster's New International Dictionary (1933) includes among definitions of the word "sale" the following: "(3) public disposal to the highest bidder; auction." An auction does not cease to be a sale merely because it is conducted by a court officer instead of the owner. From the purchaser's standpoint, someone with a right to do so has sold him the property. The fact that the purchaser at the foreclosure sale in the present case happened to be the vendor under the foreclosed contract is of no significance. Cf. *Helvering* v. *Midland Ins. Co.*, 300 U. S. 216.

We submit that it is equally clear that the taxpayer's loss resulted "from" the sale and not from the extinction of her title by an adverse judicial proceeding without consideration. The important thing transferred by the sale was the beneficial ownership, that is, the right to possession and the

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[3] The Bureau of Internal Revenue has been consistent in ruling that a loss sustained upon foreclosure sale is a capital loss. I. T. 3135, 1937–2 Cum. Bull. 226; G. C. M. 12737, XIII–1 Cum. Bull. 120. And see G. C. M. 19367, 1937–2 Cum. Bull. 115.

rents and profits. This was enjoyed by the taxpayer and her associates until the sale, or so it must be assumed in the absence of contrary proof. The vendor under the land contract possessed at most only a security title. The purchaser at a foreclosure sale is not interested in buying a security interest; he is interested in acquiring the unencumbered beneficial ownership. In *Lutz* v. *Dutmer,* 286 Mich. 467, 484, 282 N. W. 431, it was said that a foreclosure proceeding upon a land contract "* * * gives the vendor a decree for money due * * * and, by sale of the equitable title of the vendee, subjects the premises to the payment of the same," citing *Gray* v. *Hill,* 105 Mich. 189. Again at page 487, the court spoke of the "sale of his [the vendee's] equitable interest in the land," to satisfy the debt.

Thus it is apparent that the taxpayer's beneficial ownership was transferred by a sale to another and was not extinguished. Furthermore, it was obviously not the judicial proceeding which transferred that interest. The foreclosure proceeding was merely the means by which the creditor was able to have the beneficial ownership sold and transferred from the taxpayer and her associates to a new owner. The foreclosure proceeding did not deprive the taxpayer and her associates of the right to the use of the property or the right to have the sale price applied in reduction of their obligation. It took the sale to accomplish that result.

3. In deciding that the loss did not result from a "sale" the court below evidently was influenced by its conclusion that the vendor could have deprived the taxpayer and her associates of their interest in the property by declaration of forfeiture and that the only additional advantage of foreclosure was to obtain a deficiency judgment. (R. 18.) But in Michigan a court of equity will not enforce a forfeiture and hence the vendor's right to declare one can come only from an express contract provision. *Fitzhugh* v. *Maxwell, supra; Walker* v. *Casgrain, supra.* The court below relied upon *Chicago Boulevard Land Co.* v. *Apartment Garages,* 245 Mich. 448, 222 N. W. 697, which speaks of the vendor's right to declare a forfeiture when the contract contains "the usual forfeiture clause." (245 Mich., p. 450.) The court below overlooked the fact that there is nothing in this record to show that the land contract, which was foreclosed, not terminated, contained a forfeiture clause. But even if it did, it would be immaterial, for there was in fact no forfeiture. Cf. *Davidson* v. *Commissioner,* 305 U. S. 44, 46; *Helvering* v. *Midland Ins. Co., supra; United States* v. *Phellis,* 257 U. S. 156, 172.

The court below is clearly wrong in its belief that no consideration passed to the taxpayer and her associates as a result of the sale of the property. The sale not only transferred their beneficial ownership to another, but it also fixed the price which the property brought (the "amount

realized" upon the sale, as referred to in Section 111 (a), Appendix, *infra*), which price was applied in reduction of their indebtedness to the vendor, a consideration moving directly to them. *Helvering* v. *Midland Ins. Co., supra.* In this respect the situation is substantially the same as that in which a mortgagor sells the property and uses the proceeds in payment of the debt, or transfers the property to the mortgagee in extinguishment of the debt. Such cases, it has been held, are covered by Section 117. *Rogers* v. *Commissioner,* 103 F. (2d) 790 (C. C. A. 9th), certiorari denied, 308 U. S. 580; *Pender* v. *Commissioner,* 110 F. (2d) 477 (C. C. A. 4th), certiorari denied, June 3, 1940, No. 1002; *Wieboldt* v. *Commissioner,* 113 F. (2d) 384. See also *Philips* v. *Commissioner,* 112 F. (2d) 721 (C. C. A. 3d).

It may be noted that the court below relied upon (R. 18) *Commissioner* v. *Freihofer, supra,* which the Circuit Court of Appeals for the Third Circuit decided in favor of the taxpayer upon alternative grounds: first, that the foreclosure sale was not a sale within the meaning of the statute, and second that even if a statutory sale, the equity owner's loss did not result therefrom, but from the fact that his equity had become worthless, the sale being merely an identifiable event showing worthlessness. The latter ground has not been advanced by the taxpayer in the present case and did not form the basis of the court's decision. On the contrary, the court

allowed the full loss on the ground that the foreclosure established the loss but was not a sale within the meaning of Section 117 of the Act.

The fallacy of the argument that the loss in the present case resulted from worthlessness of the equity is apparent when it is remembered that the property was worth $8,000 at the time of the foreclosure (R. 13), and that the taxpayer and her associates continued to possess it with the right to any rents and profits until the sale deprived them of their beneficial ownership. Furthermore, since they were obligated under the contract, the property until the sale continued to have potential value to them by way of liquidation and application of the proceeds upon their debt. Any increase in value prior to sale would decrease or possibly even eliminate the deficiency. Even if attention is centered solely on the market value of the equity, no identifiable event occurred in the year in question which it might be urged evidenced its then worthlessness, except the sale. But the sale did not demonstrate permanent worthlessness of property retained by the taxpayer; instead it caused her loss because it disposed of her property and deprived her of the benefit of any subsequent increase in its value. Thus, it cannot be said that she suffered a deductible loss in the taxable year arising from the worthlessness of property. On the contrary, the loss resulted from the sale of the property. The argument that the loss resulted from the worthless-

ness of the equity would be equally valid in cases where the equity owner voluntarily surrenders the property to the lien holder for cancellation of the debt, and in those cases the courts have explicitly or impliedly rejected it. *Wieboldt* v. *Commissioner, supra; Rogers* v. *Commissioner, supra; Pender* v. *Commissioner, supra.*

The cases just cited, which apply the capital loss limitation, can be distinguished from the instant case only in the respect that the transactions were there undertaken by the taxpayers voluntarily, whereas here the sale was forced. This distinction underlies the point made by the court below that the taxpayer was not a party to and did not consent to the foreclosure sale. This, we submit, furnishes no basis for holding that her case is not embraced within the statutory language or intent. The court's reasoning is in effect that Section 117 of the Act covers only voluntary transactions, and not forced sales of taxpayers' properties. We contend that the statute is susceptible of no such interpretation.

The express language of Section 117 (d) is: "Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. * * *" Obviously, one may suffer a loss from a sale of his property even though it be forced and conducted by another. Thus, since the transaction in the instant case is covered by the plain language of the

statute, it is clear that no exception may be engrafted on its unambiguous terms. *Wisconsin R. R. Comm.* v. *C., B. & Q. R. R. Co.*, 257 U. S. 563, 588–589; *Crooks* v. *Harrelson*, 282 U. S. 55, 60–61; *Dimock* v. *Corwin*, reported *sub nom. United States* v. *Jacobs*, 306 U. S. 363, 373. Moreover, even if there were any ambiguity, it would have to be resolved against the taxpayer since she is claiming the benefit of a deduction. *White* v. *United States*, 305 U. S. 281, 292; *New Colonial Ice Co.* v. *Helvering*, 292 U. S. 435, 440; *Helvering* v. *Inter-Mountain Life Ins. Co.*, 294 U. S. 686, 689–690. Taking the view most favorable to the taxpayer, the clearest sort of the congressional intent would have to be shown to warrant a reformation of the statute's express language, and no such showing is possible here.

4. The legislative history prior to the Revenue Act of 1934 does not evidence any intention to limit the capital loss provisions to voluntary sales by the taxpayer. Furthermore, the reasons motivating the enactment of Section 117 of the Revenue Act of 1934, which radically changed the method of dealing with gains and losses arising from the sale of capital assets, definitely indicate a legislative intent to include all losses arising from sales of capital assets whether voluntarily made or forced upon the taxpayer.

Section 206 of the Revenue Act of 1921, c. 136, 42 Stat. 227, was the first statute to enact special

provisions with reference to capital net gains (defined as meaning the excess of capital gains over capital losses and capital deductions). It provided, subject to certain limitations, that a taxpayer might elect to be taxed on his capital net gains at 12½% instead of at the ordinary normal and surtax rates. The provision applied only to a gain arising from "a sale or exchange of capital assets"; and "capital assets" were defined generally as property acquired and held for profit or for investment for more than two years. The purpose of this provision was to permit the sale of assets held for a period of years to be effected without fear of the imposition of a prohibitive tax. It was felt that by removing the deterrent to normal capital transactions the revenue would be increased even though the tax rate upon the gain from such transactions was lowered. See *Burnet* v. *Harmel*, 287 U. S. 103, 106; H. Rep. No. 350, 67th Cong., 1st Sess., p. 10; S. Rep. No. 275, 67th Cong., 1st Sess., p. 12. The 1921 Act provided no special treatment for capital losses.

Under Section 208 of the Revenue Act of 1924, c. 234, 43 Stat. 253, a taxpayer who had realized a capital net gain was again given an election to have the tax computed at the 12½% rate. At the same time special treatment was accorded to capital net losses. Section 208 (c) had the effect of making the taxpayer pay the greater of the following taxes: (1) The tax computed by allowing the capi-

tal net losses as an ordinary deduction, and (2) the tax determined by allowing 12½% of the capital net loss to be deducted from the tax computed on the ordinary net income without the allowance of such deduction. Thus, beginning with 1924, not only were capital gains subject to tax at the flat rate of 12½%, but the amount by which the tax could be reduced by capital losses was limited to 12½% of the loss. These new provisions were enacted to provide consistency in treatment of gains and losses. See H. Rep. No. 179, 68th Cong., 1st Sess., p. 20.[4] The Revenue Acts of 1926, 1928, and 1932 made no substantial changes in the treatment of capital gains and losses.

While the purpose in enacting the capital gains provision in the 1921 Act was to encourage capital transactions by removing the deterrent effect of excessive tax burdens, there is a real doubt whether the legislature had any intention of differentiating

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[4] In *United States* v. *Pleasants*, 305 U. S. 357, this Court said (p. 360):

"There is no doubt as to the purpose of this provision as to capital net losses, which was first introduced in the Revenue Act of 1924. * * * We are told that the opportunity to minimize taxes by the practice of taking capital losses to offset ordinary net income constituted a particularly serious problem after the Act of 1921, which reduced the rate of tax on capital net gains. The results to the Treasury of that method of treating capital losses led to the adoption in the Act of 1924 of the plan for subjecting capital net losses to a limited rate in order to protect the revenues, a plan which was continued in the Revenue Acts of 1926, 1928, and 1932."

between voluntary and involuntary transactions. Involuntary transactions resulting in gains are so infrequent that it may well be doubted whether Congress considered them at all. But even if it could be assumed that Congress intended to limit that statute to voluntary transactions because of the purpose to encourage sales resulting in taxable gain, no such intention can be inferred with respect to losses under the 1924 Act. There was no purpose to encourage or discourage such transactions but merely to limit their effect as deductions from income because of the treatment which had been accorded capital gains. The capital loss provisions were inserted in the 1924 Act in fairness to the Government and not because of any considerations with respect to the character of the sale or exchange which had resulted in the loss.

Capital losses, differing in this respect from capital gains, are often occasioned by involuntary sales, but the adverse effect upon the revenues would be the same whether the capital loss arose out of a voluntary or involuntary sale. And there is no reason to suppose that Congress intended to limit the deduction upon voluntary transactions but permit a full deduction where the sale was involuntary.

Thus, prior to 1934 there is no definite expression of congressional intent that the capital loss provisions should not apply to involuntary transactions. And with the enactment of the Revenue

Act of 1934, there appears a definite expression of an intent to include involuntary transactions. The 1934 Act fundamentally changed the tax treatment of capital gains and losses. The effect of Section 117 of that Act is that for both individuals and corporations capital gains and losses are to be taken into account along with ordinary gains and losses in computing taxable net income, subject to two important limitations.

The first limitation, imposed by Section 117 (a), pertains only to individuals. Capital gain or loss is to be given tax effect only in certain percentages, depending upon the length of time that the asset had been held prior to disposition. One obvious purpose behind this provision was to "give proper recognition to the length of time during which the profit or loss has accrued"[5]—that is, to refrain from taxing the full gain or permitting deduction of the full loss in the year of realization, if the property had been held (and in all probability) appreciating or depreciating in value for some time. This purpose would seem to be unaffected by the voluntary or involuntary character of the realization.

The second limitation, imposed by Section 117 (d) and applicable to individuals and corporations alike, prevents capital loss deduction of more than

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[5] From the statement on the Senate floor by Chairman Harrison of the Senate Finance Committee. 78 Cong. Record, Part 6, p. 5846.

$2,000 in excess of capital gains. The rather obvious purpose of this restriction was to achieve safety "from a revenue standpoint, inasmuch as capital losses cannot be used to reduce ordinary income, * * *." Both limitations were expected to produce "greater stability in revenue". They were framed with the thought that "Our present system has the following defects: First. It produces an unstable revenue—large receipts in prosperous years, low receipts in depression years * * *."* And in 1934, Congress was concerned with lean rather than prosperous times. Since the depression brought on much forced liquidation resulting in capital loss, it is fair to assume that Congress wished to prevent the escape of ordinary income from taxation through deductions for such loss. And it is hardly conceivable that Congress would have intended to distinguish between "voluntary" liquidations forced by economic circum-

*The quotations in this and the two preceding sentences are from the Report of the House Ways and Means Committee on the Revenue Bill of 1934. H. Rep. No. 704, 73d Cong., 2d Sess., pp. 9, 10, Appendix B, *infra*. The report reveals purposes behind the changes wrought by Section 117 other than those mentioned in our textual discussion—for example, that to encourage normal business transactions and that to discourage the practice of taxpayers who had been taking losses within 2 years, thus getting full deductions, but taking gains after 2 years, thus getting the benefit of capital rates. That other purposes, looking toward voluntary transactions, were also behind the provision in no way limits the broader revenue-protecting purposes to which we have referred.

stances or threat of legal proceedings (as in *Rogers* v. *Commissioner, supra; Pender* v. *Commissioner, supra; Philips* v. *Commissioner, supra; Weiboldt* v. *Commissioner, supra*) and those actually carried out in legal proceedings brought by creditors.

Provisions other than Sections 117 (a) and 117 (d) of the 1934 Act reveal a congressional intention to enlarge rather than restrict the scope of the phrase "sales or exchanges." The loss sustained upon the redemption of stock (Section 115 (c), Appendix, *infra;* cf. *White* v. *United States,* 305 U. S. 281), or the retirement of bonds (Section 117 (f), Appendix, *infra*), or loss sustained by the holder of an option who fails to exercise it (Section 117 (e), Appendix, *infra*) are expressly treated as losses from a "sale" or "exchange" subject to the limitations of Section 117 (d), though they are sustained in transactions outside of the ordinary meaning of these words. Cf. *Fairbanks* v. *United States,* 306 U. S. 436. Furthermore, these examples illustrate that Congress had no intention of eliminating involuntary transactions, for many bond and stock redemptions are certainly of this character from the standpoint of the holder of the security.

These illustrations indicate quite clearly that at no time in the history of the capital loss provisions has Congress had in mind any limitation upon the meaning of "sales or exchanges" such as would be required by a distinction between voluntary and in-

voluntary transactions. Rather, the intention was progressively manifested to include within the phrase "sales or exchanges" transactions which, although not strictly sales or exchanges, were sufficiently similar in result to be classified as such. The broadening of the scope of the capital loss provisions was carried still further in the Revenue Act of 1938, c. 289, 52 Stat. 447. Section 23 (k) (2) of that Act provides that if securities were ascertained to be worthless and charged off within the taxable year and were capital assets, the loss resulting therefrom shall, except in the case of a bank, be considered as a loss arising from a sale or exchange. Losses of such character are of course purely involuntary. It would seem evident that Congress did not intend to deal more strictly with losses from worthless stock than with losses from sales of stock. Consequently, it may be assumed that if Congress had thought of the term "sales or exchanges" theretofore used in Section 117 (d) as excluding involuntary sales, it would in the 1938 Act have included such sales by express reference. Instead, Section 117 of the 1938 Act makes no change in the use of the phrase "sales or exchanges."

The legislative history thus indicates that Congress intended no exception for involuntary sales. Certainly no intention to provide such exception can be spelled out with sufficient clarity to warrant

a limitation upon the express language of the statute.[7]

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[7] A theory that the committee reports show a purpose to limit the application of Section 117 of the Revenue Act of 1934 to voluntary sales or exchanges was advanced in *Commissioner* v. *Freihofer*, 102 F. (2d) 787 (C. C. A. 3d), as follows (pp. 789–790):

"The reason for this change appears from the following excerpts from the report upon the bill of the Committee on Ways and Means of the House of Representatives:

* * * * *

"'* * * Your committee recommends the following plan:

"'First: To measure the gain or loss from the sale of property by an individual according to the length of time he has held the property, only the following percentages of the recognized gain or loss are taken into account for tax purposes: * * *.'

"The Committee said that the plan of taxation contained in the act was 'to measure the gain or loss from the sale of property by an individual according to the length of time he has held the property.' It would be difficult to find a clearer statement of the Congressional intent than this. We think it compels the conclusion that the sales of capital assets referred to in Section 117 are those sales only which are voluntarily made by a taxpayer and that judicial sales made by the sheriff in execution of a judgment in a proceeding for the foreclosure of a mortgage given by a prior owner are not included."

The court attached an improper significance to the phrase "by an individual" as thus used by the committee. The reference to an individual rather obviously was not made to indicate a preference for voluntary, as distinguished from involuntary sales, but to classify the percentage limitations proposed as inapplicable to corporations. Corporations are covered by Section 117 (d) but not by Section 117 (a). That the committee's language was inartistic appears from its omission of the statutory words "or exchange" after the

5. Apart from the legislative history, it is inherently improbable that Congress intended to refer only to losses from "voluntary" sales or sales "by the taxpayer." Rather clearly, no such limitation was intended upon the words "gain [or loss] from the sale or other disposition of property" used in Section 111 (a) of the Revenue Act of 1934, Appendix, *infra*, which prescribes the method for calculating the amount of gain or loss. If Section 111 (a) covers a sale or other disposition of the taxpayer's property at the instance of the taxpayer's creditors, without circumscription by such words as "by the taxpayer" or "voluntarily," there would seem to be no basis for presuming that Congress intended these words to be interpolated to limit the words "losses from sales or exchanges" used in Section 117.

Furthermore, if such an interpolation is to be made, grave doubts would arise as to its extent and meaning and serious administrative problems might result—none of which Congress could be presumed to intend. For example, the question would arise whether a sale conducted by a mortgagee or trustee under an express power in the mortgage should be deemed voluntary or involun-

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word "sale" and its use of the word "property" rather than the statutory words "capital asset." The portion of the committee report thus relied upon by the Third Circuit is rather an illustration than an attempt carefully to define the exact limits of the statute.

tary.[8] Should a pledge to a friendly creditor with the avowed purpose of letting him foreclose and sell, in order to avoid the disadvantages of volition, be permitted to escape the statute? If this last question were answered in the affirmative, circumvention of the statutory limitation would be quite simple[9]—if in the negative, an investigation of the

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[8] In *Commissioner* v. *Electro-Chemical E. Co.*, 110 F. (2d) 614 (C. C. A. 2d), the court said (p. 616):

"We should be surprised if a taxpayer who had pledged securities with a broker and had them sold out on the Stock Exchange could obtain a deduction of more than $2,000 for a capital loss incurred through such a liquidation. If the sale were made at the pledgor's request it could not be doubted that 117 (d) would apply and that no loss in excess of $2,000 could be deducted for income tax purposes. *Rogers* v. *Commissioner*, 9 Cir., 103 F. (2d) 790. Likewise, if the customer realized a gain through such a liquidation he would be entitled to limit his taxable gain in computing net income to the percentages provided by Section 117 (a), 26 U. S. C. A. Int. Rev. Acts. It cannot be supposed that it would make any difference whether a pledgee ordered or merely suffered his securities to be sold by his broker, and we think that in either event he could limit his taxable gain by the percentages under Section 117 (a) and could take a deduction of only $2,000 for any loss that he might suffer. We see no valid distinction between a sale by a broker who holds his customer's securities and a sale of mortgaged real estate by means of a decree in foreclosure."

[9] In *Woolford Realty Co.* v. *Rose*, 286 U. S. 319, this Court said (p. 330):

"The mind rebels against the notion that Congress * * * was willing to foster an opportunity for juggling so facile and so obvious. * * * True, of course, it is that in a system of taxation so intricate and vast as ours there are many other loopholes unsuspected by the framers of the

purpose behind every foreclosed pledge and mortgage would be required of the Commissioner. The interpretation of the court below converts a simply and clearly worded statute into a matter of uncertainty and doubt.

In *McClain* v. *Helvering* and *Helvering* v. *Thomson* (Nos. 55 and 58, present Term), the Government is contending that a partial payment and discharge of an obligation in an effort to rehabilitate a political subdivision or to reorganize a corporation is a "retirement" of the obligation within the meaning of Section 117 (f) of the Revenue Act of 1934. But even if this Court should adopt the taxpayers' argument in those cases that the word "retirement" in its ordinary meaning imports a voluntary act, it need not decide against the Government in the instant case. For a loss clearly may result "from" a "sale" of one's property within the ordinary meaning of the quoted words, even though it be a forced sale; and any holding to the contrary would have to rest upon an interpretation of the statutory language that restricts its usual meaning.

We submit that the statutory language was not used in a restricted sense; that it contemplates involuntary as well as voluntary losses from the sale

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statute, many other devices whereby burdens can be lowered. This is no reason, however, for augmenting them needlessly by the addition of another."

of property, and that the taxpayer in this case sustained a capital loss which resulted from a sale within the meaning of Section 117 (d) of the Revenue Act of 1934.

CONCLUSION

The decision of the Circuit Court of Appeals is erroneous and should be reversed.

Respectfully submitted.

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APPENDIX A

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(e) *Losses by Individuals.*—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

* * * * *

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business; or

* * * * *

(j) *Capital Losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent provided in section 117 (d).

* * * * *

[U. S. C., Title 26, Sec. 23.]

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) *Computation of Gain or Loss.*—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

* * * * *

[U. S. C., Title 26, Sec. 111.]

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

* * * * *

[U. S. C., Title 26, Sec. 113.]

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

* * * * *

(c) *Distributions in Liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. Despite the provisions of section 117 (a), 100 per centum of the gain so recognized shall be taken into account in computing net income. In the case of amounts distributed (whether before January 1, 1934, or on or after such date) in partial liquidation (other than a distribution within the provisions of subsection (h) of this section of stock or securities in connection with a reorganization) the part of such distribution which is properly chargeable to capital account shall not be considered a distribution of earnings or profits within the meaning of subsection (b) of this section for the purpose of determining the taxability of subsequent distributions by the corporation.

* * * * *

[U. S. C., Title 26, Sec. 115.]

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *General Rule.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net income:

100 per centum if the capital asset has been held for not more than 1 year;

80 per centum if the capital asset has been held for more than 1 year but not for more than 2 years;

60 per centum if the capital asset has been held for more than 2 years but not for more than 5 years;

40 per centum if the capital asset has been held for more than 5 years but not for more than 10 years:

30 per centum if the capital asset has been held for more than 10 years.

(b) *Definition of Capital Assets.*—For the purposes of this title, "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business.

* * * * *

(d) *Limitation on Capital Losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. If a bank or trust company in-

corporated under the laws of the United States or of any State or Territory, a substantial part of whose business is the receipt of deposits, sells any bond, debenture, note, or certificate or other evidence of indebtedness issued by any corporation (including one issued by a government or political subdivision thereof), with interest coupons or in registered form, any loss resulting from such sale (except such portion of the loss as does not exceed the amount, if any, by which the adjusted basis of such instrument exceeds the par or face value thereof) shall not be subject to the foregoing limitation and shall not be included in determining the applicability of such limitation to other losses.

(e) *Gains and Losses from Short Sales, Etc.*—For the purpose of this title—

(1) gains or losses from short sales of property shall be considered as gains or losses from sales or exchanges of capital assets; and

(2) gains or losses attributable to the failure to exercise privileges or options to buy or sell property shall be considered as gains or losses from sales or exchanges of capital assets held for one year or less.

(f) *Retirement of Bonds, Etc.*—For the purposes of this title, amounts received by the holder upon the retirement of bonds, debentures, notes, or certificates or other evidences of indebtedness issued by any corporation (including those issued by a government or political subdivision thereof), with interest coupons or in registered form, shall be considered as amounts received in exchange therefor.

[U. S. C., Title 26, Sec. 101.]

APPENDIX B

H. Rep. No. 704, 73d Cong., 2d Sess. (pp. 9–10, 30–32):

* * * * *

Existing law provides in section 101 for a special treatment of the gains and losses resulting from the sale of capital assets held over 2 years. The tax on gains on such sales is limited to 12½ percent, with a corresponding limitation in case of losses. In the case of assets held less than 2 years, the gains are taxed in full and the losses allowed in full except in the case of stocks and bonds, losses from which are limited under section 23 (r).

Our present system has the following defects:

First. It produces an unstable revenue—large receipts in prosperous years, low receipts in depression years.

Second. In many instances, the capital-gains tax is imposed on the mere increase in monetary value resulting from the depreciation of the dollar instead of on a real increase in value.

Third. Taxpayers take their losses within the 2-year period and get full benefit therefrom, and delay taking gains until the 2-year period has expired, thereby reducing their taxes.

Fourth. The relief afforded in the case of transactions more than 2 years is inequitable. It gives relief only to the larger taxpayers with net incomes of over $16,000.

Fifth. In some instances, normal business transactions are still prevented on account of the tax.

Your committee has examined the British system, which disregards these gains and losses for income-tax purposes. The stability of the British revenue over the last 11 years is in marked contrast to the instability of our own. In that period the maximum British revenue was only 35 percent above the minimum, while in our own case the percentage of variation was 280 percent.

Your committee, however, has been unable to reach the conclusion that we should adopt the British system. It is deemed wiser to attempt a step in this direction without letting capital gains go entirely untaxed. Your committee recommends the following plan:

First. To measure the gain or loss from the sale of property by an individual according to the length of time he has held the property, only the following percentages of the recognized gain or loss are taken into account for tax purposes:

One hundred percent if the capital asset has been held for not more than 1 year;

Eighty percent if the capital asset has been held for more than 1 year but not more than 2 years;

Sixty percent if the capital asset has been held for more than 2 years but not more than 5 years; and

Forty percent if the capital asset has been held for more than 5 years.

* * * * *

It is believed that the adoption of this plan (see sec. 117 of the bill) will result in much greater stability in revenue, will give all taxpayers equal treatment, will encourage

normal business transactions, and will yield substantially greater revenue. The method proposed is safe from a revenue standpoint, inasmuch as capital losses cannot be used to reduce ordinary income, while gains are taxed in full or in part in proportion to the time for which the property has been held. The existing method which has been in force since 1921 can be defended only on the ground of expediency.

* * * * *

Section 117. Capital gains and losses: This section provides for the new treatment of capital gains and losses already described in general terms under item (3) of the first part of this report. It should be borne in mind that this new treatment supersedes the 12½ percent capital gain and loss system of present law, as well as the system of limiting short-term losses to the amount of short-term gains as provided for under section 23 (r), (s), and (t) of the Revenue Act of 1932.

The following propositions are essential to the consideration of the new treatment:

1. The determination of the amount of gain or loss from each sale or exchange of property, the recognition of such gain or loss, and the basis for determining gain and loss, are all provided for in sections 111, 112, and 113 of the bill. These sections correspond to the same numbered sections of existing law.

2. Section 117 of the bill deals with the manner of taking into account in computing net income these gains and losses which have been determined under section 111 and have been recognized under section 112.

3. Subsection (a) provides for all taxpayers, other than corporations, a series of per-

centages which must be used in arriving at the amount of the recognized gain or loss which shall be taken into account in computing net income. The theory is that the gain or loss should be somewhat reduced in proportion to the time for which the capital asset has been held.

* * * * *

To illustrate the application of the new capital gain-and-loss system in the case of an individual, the following example is given:

Item	Gain recognized under sec. 112	Loss recognized under sec. 112	Time held	Percent applicable	Gain taken into account under sec. 117	Loss taken into account under sec. 117
Corporate stock	$5,000		9 months	100	$5,000	
Bonds		$4,000	1½ years	80		$3,200
Government bonds	1,000		2½ years	60	600	
Real estate		3,000	6 years	40		1,200
Short sales	2,000			100	2,000	
Total					7,600	4,400

In the above case, the taxpayer would include in gross income subject to tax $7,600 in gains and be allowed to deduct $4,400 of losses. The net increase in his income will, therefore, be $3,200. If, however, in another case, the total shown in the last column of the example had been $7,600 (loss) and the total in the preceding column, $4,400 (gain), then the taxpayer would be allowed to deduct from his gross income only $4,400 out of his $7,600 of losses. Practically speaking, in such a case the gains and losses would, therefore, have no effect on the tax paid by the taxpayer.

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No. 49

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1940

GUY T. HELVERING, Commissioner of Internal Revenue,

Petitioner,

v.

GODFREY HAMMEL AND PEARL HAMMEL

Respondent.

BRIEF FOR THE RESPONDENT

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BRIEF FOR THE RESPONDENT

Questions Presented

The statement under the above caption of Petitioner's Brief (p. 2) is to our mind not sufficiently definite. We believe it should be stated as follows:

The question presented is whether the loss to the Respondent, Pearl Hammel, is a loss resulting from the "sale or exchange" of the property in question and therefore within the purview of Section 117 (d) of the Revenue Act of 1934, or, whether the loss is an ordinary loss allowable as a deduction in full under and within the purview of Section 23 (e) (2) of the Revenue Act of 1934.

Summary of Respondent's Argument

The Respondent contends that her loss was not occasioned by a "sale or exchange" *by her,* but was a forcible taking away of her equitable interest in property by virtue of foreclosure proceedings; that this loss was occasioned by economic conditions and the identifiable event establishing that worthlessness was the foreclosure proceedings, the Sheriff's sale being merely the legal means devised to measure the damage to the plaintiff and without which it would not be possible to ascertain that damage which is based on the rule of the difference between the balance owing on the contract and the fair market value of the property.

The Respondent further contends that Section 117 (d) of Revenue Act of 1934 relates solely to "sales and exchanges" of capital assets made by the taxpayer voluntarily, the words "sales and exchanges" being used in their ordinary connotation.

Respondent's Argument

A.

THE PURPOSE OF SECTION 117 IS IN GREAT PART TO PREVENT TAX AVOIDANCE.

It seems quite evident that Section 117 of the Revenue Act of 1934 was mainly designed to prevent tax avoidance by the deliberate or voluntary act of taxpayers, such as sales of stock or investments by a taxpayer for the

purpose of establishing a loss during a certain taxable year, and that it was never intended to cover a transaction in which a taxpayer sustains an involuntary bona fide loss through legal action depriving or divesting him of his property through due process of law.

In this connection we wish to call this Court's attention to House Report No. 1388 of the House Ways and Means Committee on H. R. 13,770, 67th Cong. 4th Session, and to the same account as set forth in Petitioner's Appendix B.

> "Our present system has the following defects: * * * Third: Taxpayers *take their loss* within the two year period and get full benefit therefrom, and *delay taking gains* until the two year period has expired thereby reducing their taxes."

Among the purposes of the Section the following is set forth:

> "Fourth: To prevent *tax avoidance* in the case of capital losses * * *. The changes made are either to prevent *tax avoidance* or to bring about *greater equity.*"

If Congress had intended a "sale or exchange" in Section 117 to include and cover losses suffered through foreclosure, it would have made a provision similar to the provisions of Sections 117 (e) (1) and (2) and (f) wherein "short sales" and gains or losses attributable to the failure to exercise privileges or options to buy or sell and amounts received by the holder upon the retirement of bonds, etc., though not normally within the ordinary definition of a "sale or exchange," are expressly ordered to be *considered* as gains or losses from "sales or exchanges" of capital assets.

Petitioner, in his "summary of argument" (Petitioner's Brief, p. 6) mentions the Revenue Act of 1938, with particular reference to losses from worthless securities having been expressly subjected by that Act to the capital gain and loss provisions. (Petitioner is we believe referring to Section 23 (g) (2) of the Revenue Act of 1938). He goes on to argue as follows:

> "If Congress had thought that the phrase 'sales or exchanges,' as theretofore used, had included only voluntary transactions, it probably would have expressly broadened the scope of the phrase as used in Section 117 of the 1938 Revenue Act, which it did not do."

We submit that this is not a correct deduction or inference. On the contrary, Congress having used the phrase "sales or exchanges," and having in mind the ordinary meaning of the word "sale" and of the word "exchange", expressly provides in both the 1934 Act and the 1938 Act that certain losses, which otherwise did not come within the term "sale or exchange," are *to be considered* as losses from "sales or exchanges."

This is manifest from Section 117 (e) (1) and (2) and (f) of the 1934 Revenue Act, and Section 23 (g) (2) of the 1938 Act.

That Congress must be deemed to have used the words in their ordinary signification needs no argument. *Williamson v. Berry*, 49 U. S. 495, 12 L. Ed. 1170.

Is it not, therefore, a more logical assumption that if Congress had intended that a forced divestiture of ownership of property should be considered a "sale or exchange" it would have expressly included such transaction under Section 117 or made it another exception to Section 23

by express provision, as it did with regard to the transactions above referred to.

It is significant also that Congress in enacting Section 111 of the Revenue Act of 1934 (Appendix A, Pet. Brief) used the following language:

> "The gain from the sale *or other disposition* of property shall be the excess of the amount realized therefrom * * *."

Here Congress realizing the limitations of the word "sale" expressly broadened the statute.

An excellent argument for our position is found in *Commissioner v. Freihofer,* 102 F. (2d) 787 (3d Cir.) wherein the Court said:

> "These statements which were quoted with approval by the Finance Committee of the Senate in its report upon the Bill (Senate Report No. 558, 73rd Cong. 2d Session), show quite convincingly that *it was the intent of the Congress to deal in Section* 117 *with gains and losses resulting from the voluntary sale of capital assets.* The Committee said that the plan of taxation contained in the Act was 'to measure the gain or loss from the sale of property *by an individual* according to the length of time *he has held* the property.' It would be difficult to find a clearer statement of the Congressional intent than this. We think it compels the conclusion that the sale of capital assets referred to in Section 117 are those sales only which are *voluntarily* made by a taxpayer and that *judicial sales made by the Sheriff in execution of a judgment in a proceeding for the foreclosure of a mortgage given by a prior owner are not included.*" (Italics, ours.)

Persuasive also are the excerpts from the Congressional discussion set forth in the Appendix of this brief.

Tax avoidance is almost invariably the result of the planned, voluntary act of the taxpayer. Prior to the passage of Section 117 of the Revenue Act of 1934, it was legally permissible for a taxpayer to minimize his income tax by deliberately selling stocks or other capital assets at a loss, and taking a full deduction for the loss thus established. Congress, in its desire to place as many restrictions as possible on this practice, enacted Section 117, among other provisions. Nowhere in the Act can there be found any language whatsoever to justify an inference that Congress intended anything else. Nowhere in the Act can there be found language to indicate the placing of any restrictions upon the right of the taxpayer to take full deduction for losses suffered over which he had no control, except as expressly stated in the Act, Sec. 117 (e) and (f).

That this loss was involuntary is not questioned. The proceedings were had in open court in Oakland County and appealed therefrom to the Supreme Court of the State of Michigan. The respondent's property was first foreclosed. This was followed by the Sheriff's sale, as required by law, in order that the seller might determine the amount of the deficiency and have a decree therefor against the respondent. The sheriff acted as the agent of the law (24 R.C.L., 912) and at the instance of Mrs. Julia Adams, the Seller in the land contract, she being the person whose interests were directly and completely adverse to the interests of respondent Pearl Hammel. It was not sold by the respondent. It was not a sale or exchange by the respondent, the entire proceeding being one over which the respondent had no control. Her interest in the property was "extinguished", not sold.

Nowhere in his brief does Petitioner contend that Respondent was a party to or consented to the Sheriff's sale. On the contrary he seems to concede this point. (Petitioner's Brief, p. 5.)

B.

A SALE OR EXCHANGE UNDER SECTION 117 MEANS A VOLUNTARY SALE BY THE TAXPAYER.

Inasmuch as the vital question in this case is whether the Respondent's loss was due to a "sale or exchange" within Section 117 the definitions of these words in common usage and in definitions by the Courts are of importance.

> "A sale is a contract whereby one acquires a property in the thing sold and the owner parts with it for a valuable consideration." (Words and Phrases, Vol. 4, p. 437.)
>
> "A sale is generally understood to mean the transfer of property for money." (Id. p. 441).
>
> "Sale, in the ordinary sense means transfer of property for a fixed price in money or its equivalent. * * * A sale is a contract whereby one acquires a property in the thing sold and the owner parts with it for a valuable consideration." (*Hale v. Helvering*, 85 F. (2d) 819.)

In *Pinellas Ice & Cold Storage Co.*, 21 BTA, 425, the Board states the rule laid down and recognized by this Court as to what constitutes a sale as expressed in the case of *Williamson v. Berry*, supra:

> "We remark that 'sale' is of precise legal import both at law and in equity. It means at all times a contract between parties, to give and to pass rights of property for money which the buyer

pays, or promises to pay, the Seller for the thing bought. * * * Congress should be presumed to have a knowledge of the law as laid down by the Supreme Court, long recognized as to what constitutes a sale, and we must assume that the language used in Section 203 was used in that import, especially since the Section of the Statute involved used both the words 'sale' and 'exchange'."

The opinion of the Third Circuit in the instant case aptly phrases the definition of "sale" in the following language:

> "Sale is a word of precise legal import. Its elements are (1) parties competent to contract; (2) mutual consent; (3) a thing, the absolute or general property in which is transferred from the seller to the buyer; (4) a price in money paid or promised. (*Bullen v. Thompson*, 92 U. S. 412, 414; *Williamson v. Berry*, supra.) There is nothing in the legislative history of the statute in question or in the language of the Act indicating that the Congress used the word 'sale' in any sense other than its precise legal import or plain and obvious meaning. If any one of the above elements be absent, it is not a sale as that word is understood in its ordinary signification." *Commissioner v. Hammel*, 108 F (2d) 753.

Again, in *Commissioner v. Freihofer*, 102 F. (2d) 787 (3rd Cir.), the Court said:

> "Blackstone defined a sale as 'a transmutation of property from one man to another in consideration of some price or recompense in value' 2 Bl. 446. It is a contract for the transfer of property from one person to another for a valuable consideration. See 7 Words and Phrases, First series, Sale, page 6291. There must be parties standing to each other in the relation of buyer and seller, their minds must assent to the same proposition, and a consid-

eration must pass. *Butler v. Thomson,* 92 U. S. 412, 23 L. Ed. 684. Where the word is used, in the absence of anything to the contrary it will be assumed that the word is intended to have its usual signification. *De Ganay v. Lederer,* 250 U. S. 376, 39 S. Ct. 524, 63 L. Ed. 1042; *State v. Colonial Club,* 154 N. C. 177, 69 S. E. 771, 31 L.R.A.N.S., 376, Ann. Cas. 1912A, 1079. That signification includes voluntary action by the owner and a consideration. Here the taxpayer, the owners of the properties involved in the foreclosures, were not parties to the sheriff's sales, nor did they receive any part of the price obtained at those sales. These were, therefore, not sales in the ordinary sense. On the contrary they were adverse judicial proceedings whereby the titles of the taxpayers were extinguished, as we shall presently point out, without any recompense."

In *Mont Echols,* 24 BTA, 1127, the Board states:

"On the other hand, we cannot find in the capital gain and loss provision of the Act, *nor in the legislative history* of their enactment, any intent to include in capital losses, losses sustained by capital assets merely becoming worthless. The intent there is clearly to allow as capital losses only those occuring from 'sale or exchange' of capital assets. Losses due to such assets becoming worthless being covered by the ordinary loss provision allowing their deductions from income other than that represented by capital gain." (Italics ours.) See also *Dallas Transfer & Terminal Warehouse Company v. Com.,* 70 F (2d) (20) 95.

We submit that the foregoing decisions conclusively establish

(a) that the phrase "sale or exchange" as used in the Act is to be taken in its ordinary connotation;

(b) that a *sine qua non* of a "sale or exchange" is the volition of the seller and his consequent participation as one of the parties to the transaction, and

(c) that the words exclude any taking away or divesting of the property of an owner by process of law, in which instance the owner's consent is lacking.

There seems to be no contention that the transaction here involved constitutes an "exchange" and we content ourselves with but two definitions:

> "Exchange is defined as a mutual grant of equal interest, the one in consideration of the other." (Hale v. Helvering, supra).
>
> "Exchange is a mutual transfer of property other than for money."
>
> (Law v. McLaughlin, 2 F, Supp. 601, 603).

The Board of Tax Appeals has consistently held transactions like the present not to be "sales or exchanges." Characteristic decisions are the following:

> *Warfield v. Comm.*, 38 B. T. A., 907;
> *Rust, Jr. v. Comm.*, 38 B. T. A., 910;
> *Hill v. Comm.*, 40 B. T. A., 376;
> *Ganopuls v. Comm.*, 39 B. T. A., 1120;
> *Nebraska Bridge etc. Co. v. Comm.*, 40 B. T. A., 40;
> *Hoffman v. Comm.*, 40 B. T. A.
> *Gransden v. Comm.*, 39 B. T. A. 985.

Under the above definitions and decisions, to whom did Mrs. Hammel part with her interest in this property for a valuable consideration?

To whom did she give title?

What was the value or consideration passing to her?

If, as stated in *U. S. v. Benedict,* 280 Fed. 76, 80, the word "sale" in its ordinary sense means a transfer of property for a fixed price in money or its equivalent, where was the transfer of property and where was the money or its equivalent passing to Mrs. Hammel?

Congress is presumed, under the decisions, to use certain words in their ordinary meaning. Can this Court, by any stretch of the imagination, decide that Mrs. Hammel sold this property? Can the Court say this was a sale? To give a practical illustration: Suppose a person has lost his home by foreclosure and after the foreclosure is complete, testifies in court that he sold his home. Would he be telling the truth or would he be telling a falsehood? To call the transaction, which actually took place here, a sale or exchange is straining the word "sale" and the word "exchange" beyond any meaning that we have ever read of or heard of.

An "exchange" is a mutual grant of equal interest, the one in consideration of the other (*Hale v. Helvering.*) If this transaction be a mutual grant of equal interest, then the words "mutual" and "grant" are clearly dragged out of their proper sphere of meaning to suit the wishes of the petitioner. There was no grant on the part of the respondent. She gave no deed. She gave no assignment, nor did the vendor in the contract give anything whatsoever to the respondent. The respondent's property *was taken from her. It was foreclosed.* It was *not sold.* It was *not exchanged,* and she received nothing whatsoever. Her interest was "extinguished", not sold. The deficiency judgment against her was, of course, less by the amount of the bid at the

Sheriff's sale, but that does not mean that the respondent received anything.

We are not claiming the deficiency judgment, amounting to $79,000.00, *as a loss,* and we direct the Court's attention to the fact that, regardless of the amount of the deficiency judgment, the loss was the amount of money she paid on the contract, to-wit: $4,998.03, *and that amount was not in any way affected by the amount of the deficiency judgment.*

Where was there any mutual grant of equal interest?

What grant of any equal interest passed to Mrs. Hammel in this transaction?

What grant was made by Mrs. Hammel for an equal interest?

It is only by a *violent straining of the language,* and by *ignoring the purposes* of Section 117 that the taxpayer could be held to have been a participant in either a "sale or an exchange."

Lynch v. Alworth-Stephens Co., 267 U. S. 364-370 (45 S. Ct. 274, 69 L. Ed. 660) holds:

> "The plain, obvious and rational meaning of a statute is always to be preferred to any curious, narrow, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover."

This is the rule applied to the taxing acts.

See also *Burkett v. Comm.,* 31 F (2d) 667 and *Burnet v. Harmal,* 287 U. S. 103, 74 L. Ed. 199.

What occurred was exactly this: The Seller in the land contract decided to reposses herself of her property, commenced foreclosure proceedings against the Syndicate owners (respondent being one of them) and obtained a decree of foreclosure authorizing a public sale to determine whether any deficiency existed upon which a deficiency judgment or decree could be based against the Syndicate members. The Syndicate members were unable to pay. Therefore, what happened was: a *forcible, legal taking away* of the Syndicate Members' rights to the property *without their consent* and, as a matter of fact, against their active opposition in Court. It is stipulated that in the year 1934, Respondent lost her interest in this property. (R. p. 13).

We are aware that in *Commissioner v. Electro-Chemical Co.*, 110 F. (2d) 614, the Court takes the position that if it is held that Section 117 pertains only to voluntary sales by the taxpayer, connivance between a seller and a purchaser, or between a mortgagor and mortgagee, or between a client and his broker, could deprive the government of revenues. Petitioner in his Brief (p. 25) says substantially the same thing.

Since when are the Courts justified in a forced or unnatural construction of a statute for such a reason. By the same specious reasoning even prayer to the Almighty could be condemned just because men have occasionally become crazed through incessant and inordinate recourse to that medium of communication with their Creator.

We take it that the bona fides of every transaction which comes under the scrutiny of the Internal Revenue Department is established to the satisfaction of the department or of the Courts before the taxpayers contention is allowed to prevail. There can be no question of

the honesty and good faith of the transaction here in issue. No question has ever been raised in this case on such grounds at any stage of a long drawn out process of litigation.

The Electro-Chemical case recites that the proceeds of the mortgage foreclosure sale "must be deemed in full satisfaction of the mortgage debt and no right to recover any deficiency in any action or proceeding shall exist." This because the owner of the mortgage did not attempt to enforce the deficiency against the taxpayer. In the instant case the taxpayer was forced into bankruptcy to escape collection of the deficiency.

We submit that the opinion last referred to is not the correct solution of the legal problem there in issue.

C.

THE LOSS OF RESPONDENT WAS DUE TO ECONOMIC CONDITIONS WHICH MADE HER INTEREST WORTHLESS AND THE FORECLOSURE DECREE WAS THE IDENTIFIABLE ACT WHICH MERELY PROVED RESPONDENT'S LOSS.

In order that we may properly approach the question whether the loss of Respondent was brought about or resulted from the "sale or exchange" of her interest in the property within the meaning of Section 117 of the 1934 Revenue Act, it is well to inquire what was the exact situation confronting her immediately prior to the trial of the foreclosure action.

According to the Stipulation of Facts (R. pp. 12-14), the syndicate of which the Respondent was a member purchased the land here in question on land contract, the purchase price being $96,000.00. Including the down pay-

ment, $24,000.00 had been paid on principal by 1934, leaving an unpaid principal balance in 1934 of $72,000.00, plus interest and State and County taxes for several years.

Because of the general financial condition of the country the total value of this land receded to the value of ordinary farm land and its market value in 1934 was approximately $8,000.00 instead of $96,000.00 which was the contract price. (Stipulation of Facts, R. pp. 12 and 13).

The members of the syndicate, including the Respondent, were unable to meet the payments called for by the contract and were in default.

It is apparent that the interest of the syndicate members under this contract in 1934 immediately prior to foreclosure proceedings was entirely worthless. Considering that the total property was worth $8,000.00, nevertheless the interest of the syndicate members, inasmuch as they owed a balance of over $72,000.00, must have been utterly worthless, and it is impossible to conceive of anyone being willing to pay any sum whatsoever for the interest of the syndicate members under their contract.

If the estate of A has assets of $8,000.00 and liabilities of $72,000.00, what is A's estate worth, or what is its fair market value? Precisely nothing minus. The estate is insolvent.

This answers the argument of Petitioner on the subject of worthlessness. (Petitioner's Brief, p. 13).

Petitioner states (Pet. Brief p. 12) that worthlessness of the property was not advanced by the Respondent in

this case. That question has always been and now is in the case. (See Petition for Redetermination, par. 8, R. p. 3).

Her interest being worthless, it would have been to the advantage of respondent to abandon the property, and had she abandoned it, even with the consent of the seller, and had she been able to establish in Court proceedings the finality of that abandonment, she would have been entitled, under Section 23 (e) (2), to deduct the loss in full for the year 1934.

It is a fair and logical assumption, well within the stipulation of facts, to conclude that Respondent was not allowed, so far as the seller was concerned, to abandon her interest, because the seller commenced foreclosure proceedings in which she sought to take away respondent's interest in the property and to obtain a deficiency judgment. By the decree, the Court found that the syndicate members were indebted to the plaintiff for the full unpaid balance and interest evidenced by said contract and ordered payment thereof, and provided that in default of said payment the land be sold at public auction.

The foreclosure sale did not occasion that worthlessness and it did not occasion that loss. World wide circumstances ante-dating the foreclosure sale was the factor because of which this Respondent had lost whatever she had put into the property.

It is stipulated that the decree of foreclosure gave no right of redemption. Therefore, the decree itself became immediately the identifiable act which conclusively established the fact of loss in the year 1934. It is stipulated that the total land purchased was worth in 1934 only $8,000.00. It is stipulated that the plaintiff obtained

a deficiency judgment against all members of the syndicate, jointly and severally, of approximately $79,000.00. Unless we are to indulge in the violent assumption that land concededly worth only $8,000.00 might bring at a sale $79,000.00, it became definitely established the moment the decree was signed that the entire investment by the members of the syndicate, including this Respondent, was utterly wiped out. The sale which the decree ordered, was and always is, designed solely for the purpose of determining the amount in which the defendant is to be penalized in addition to the loss of defendant's interest in the property.

A foreclosure sale is, therefore, merely a part of the machinery through which a vendor, bringing action in equity for foreclosure of the vendor's lien and deficiency decree may have determined the exact amount of that defeciency, a sale being the only means of making effective the rule that the vendor is entitled to the difference bebetween the balance due upon the contract and the fair market value of the property. As was said in *Chicago Boulevard Land Company v. Apartment Garages*, 245 Mich. 448-450:

> "The contract contained the *usual provision* that on default of the vendee the vendor had the right to declare the contract void, retain moneys paid and improvements and re-take possession. * * * On vendee's default in a land contract containing the usual foreclosure clause, vendor may treat the contract as continuing in force and sue at law upon it for payments due, or bring action in equity for foreclosure of the vendor's lien and deficiency decree; or he may declare it forfeited."

Now, the type of land contract in question here is not described in the stipulation of facts. The instrument is

described merely as a land contract. Had there been any question in the minds of either party at the time of the stipulation that the type of land contract mattered, it would have been very easy either to describe it in the stipulation or to set it forth in full. It is evident, therefore, we submit, that it was the usual form of land contract and, as stated above, a forfeiture provision is a usual provision in land contracts in Michigan. And we submit, therefore, that it should be presumed that the vendor in this case had the right to declare a forfeiture if she so wished.

However, once the vendor declares a forfeiture she is forever barred from suing upon the contract either at law or in equity for payments due. (*Chicago Boulevard Land Co. v. Apartment Garages,* supra.)

If Petitioner's argument is sound, then one who is deprived of his land contract interest by a notice of forfeiture (there being no sale under such a proceeding) may take a deduction in full under Section 23 of the Revenue Act of 1934.

However, if the purchaser (helpless in the matter), is subjected to an equity foreclosure, he loses his interest and in addition suffers a deficiency decree which may (and in this case did) result in bankruptcy.

Then merely because his property, without his consent, is sold by the Sheriff or Commissioner, he is limited in the amount of loss he may claim in his income tax return by the provisions of Section 117.

Why the additional hardship placed upon the one who suffers the greater misfortune?

Despite Petitioner's argument, it follows that the Sixth Circuit was correct when, in its opinion, in the instant case it said:

> "It follows that the vendor here in question had the right to deprive the Respondent and her joint adventurers of all interest in the property by a declaration of forfeiture and the only additional advantage of foreclosure was to obtain a deficiency judgment. (*Commissioner v. Hammel,* supra.)

While it may be beside the point, even had there been a period of redemption allowed the Respondent after the foreclosure sale, the loss would not have arisen from the sale. The loss would then have been determined by the expiration of the period of redemption, and again the sale would merely have been the measuring stick of the damages of the vendor. (*Commissioner v. Hawkins,* 91 F. (2d) 354.

We submit, therefore, that by no process of reasoning can it be said that this was a loss arising from the sheriff's sale.

Petitioner needlessly argues that a Sheriff's sale is a sale. Certainly it is a sale, but it is not a sale by the taxpayer, and it is not a sale within Section 117 of the Revenue Act of 1934.

Petitioner devotes considerable attention to the nature of the interests which are created upon the execution of a land contract, and with his conclusions we have very little quarrel. The cases cited by him establish the fact that while the vendor still retains the legal title, the vendee has the equitable title and consequently the beneficial ownership, including the right to possession, and the right to the rents and profits and the power, unless

expressly forbidden by the terms of the contract, to transfer those rights to others. We concede that the so-called beneficial ownership of the Respondent under land contract was a capital asset and that consequently her loss was the loss of a capital asset. But to argue, as Petitioner does, that because the Respondent had the right to sell or otherwise dispose of her beneficial ownership or interest, and that that interest and the property in which the interest lay was sold at a Sheriff's foreclosure sale that, therefore, the loss arose from the sale, is a complete *non sequitur*. (Petitioner's brief, pp. 7-8).

Whether the Sheriff's sale disposed of the property, or of the Respondent's beneficial interest therein, or whether that sale was a sale of the equitable title of the vendee is unimportant, because as a matter of hard fact the loss was occasioned by economic conditions beyond the control of the Respondent which rendered her interest worthless. The foreclosure was merely the identifiable event which established her loss. She was deprived of her interest in the property not by sale but, as was said by the Sixth Circuit, by an adverse judicial proceeding which completely extinguished her title without consideration.

Conclusion

It is apparent that this transaction insofar as Respondent is concerned was not a sale or exchange of property; that the loss was not the result of any voluntary act upon the part of the Respondent, and that it was the result of Respondent's interest becoming worthless, which worthlessness was merely proven by the foreclosure proceedings.

Respondent's loss, therefore, is in the same category as any loss over which a taxpayer has no control, such as those losses which are due to the act of God, casualty, or assets becoming worthless, which are the types of loss contemplated by and within the purview of Section 23 of the 1934 Act. That Section also provides, under subsection (e) (2) thereof, that losses by individuals, if incurred in *any* transaction entered into for profit, though not connected with a trade or business, are deductible in full.

We respectfully submit that the opinion of the Circuit Court of Appeals is correct and should be affirmed.

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Dated: Nov. 2, 1940.

Appendix

CONGRESSIONAL DISCUSSION (House)
(Cong. Rec. Vol. 78)

Mr. Cooper of Tennessee. * * * Under existing law there are only two types of capital gains and losses treated under the income tax law. We will consider for a moment a capital gain-or-loss transaction. If the asset has been held for less than 2 years it is treated in full as ordinary income. The full amount is taken by way of tax on the gain and a full amount given by way of loss on the loss sustained. But if the asset is held over 2 years there is a rate of 12½ percent applied to the capital gain or the capital loss. This simply means that many *wealthy taxpayers* of this country *dispose* of their capital assets in order to get the benefit of the loss by selling just before the 2-year period expires and the gain *by selling* just over the 2-year period. Your committee, after giving most thoughtful attention to the subject, decided that there should be a further extension or division of the period of time within which treatment should be given to these capital gains or losses. (P. 2789).

CONGRESSIONAL DISCUSSION (House)
(Cong. Rec. Vol. 78)

Mr. Arnold. Then if I should hold some stocks for a period of 2 years and *I should sell* that stock at a loss and I did not have any income to offset that from other stocks, would I entirely lose the benefit of that credit?

Mr. Samuel B. Hill. You would lose it entirely.

Mr. Vinson of Kentucky. May I suggest that under the existing law you lose the right *to take a loss* on the sale of stock against an ordinary gain?

Mr. Arnold. Under existing law?

Mr. Vinson of Kentucky. That was put into the 1932 Revenue Act.

Mr. Samuel B. Hill. The committee feels *it has absolutely plugged that avenue* through which taxes were escaping *by manipulation of capital investments, purely for the purpose of creating paper losses in order that they might offset those losses against ordinary income, and thereby reduce the taxes of the taxpayer.* I think we have completely blocked that loophole of tax escape, and that is one of the large leaks we had to deal with. (P. 2663).

CONGRESSIONAL DISCUSSION (House)
(Cong. Rec. Vol. 78)

Mr. Harrison. * * * The attention of the taxpayers of the United States has, however, been directed to numerous instances of wealthy individuals who have completely eliminated their income taxes *by taking losses* on sales of stock made to members of the taxpayer's family or to business associates. Frequently the taxpayer has reacquired the securities within a short time after the sale. In other words, *the sale was simply for the purpose of taking a tax loss;* and in many instances, after the transaction was concluded, the taxpayer held precisely the same property as before.

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SUPREME COURT OF THE UNITED STATES.

No. 49.—October Term, 1940.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, *vs.* Godfrey Hammel and Pearl Hammel. } On Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit.

[January 6, 1941.]

Mr. Justice Stone delivered the opinion of the Court.

We are asked to say whether a loss sustained by an individual taxpayer upon the foreclosure sale of his interest in real estate, acquired for profit, is a loss which, under § 23(e)(2) of the 1934 Revenue Act, 48 Stat. 680, may be deducted in full from gross income for the purpose of arriving at taxable income, or is a capital loss deductible only to the limited extent provided in §§ 23(e)(2), (j), and 117.

In the computation of taxable income § 23(e)(2) of the 1934 Revenue Act permits the individual taxpayer to deduct losses sustained during the year incurred in any transaction for profit. Subsection (j) provides that "losses from sales or exchanges of capital assets" shall be allowed only to the extent of $2,000 plus gains from such sales or exchanges as provided by § 117(d). By § 117(b) it is declared that "capital assets" "means property held by the taxpayer . . . but does not include stock in trade of the taxpayer . . . or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

Respondent taxpayers, with other members of a syndicate, purchased "on land contract" a plot of land in Oakland County, Michigan, for the sum of $96,000, upon a down payment of $20,000. The precise nature of the contract does not appear beyond the fact that payments for the land were to be made in installments, and the vendor retained an interest in the land as security for payment of the balance of the purchase price. Before the purchase price was paid in full the syndicate defaulted on its payments. The vendor instituted foreclosure proceedings by suit in equity in a state court which resulted in a judicial sale of the property, the vendor be-

coming the purchaser, and in a deficiency judgment against the members of the syndicate. Respondents' contribution to the purchase money, some $4,000, was lost.

The commissioner, in computing respondents' taxable income for 1934, treated the taxpayers' interest in the land as a capital asset and allowed deduction of the loss from gross income only to the extent of $2,000 as provided by §§23(j) and 117(d), in the case of losses from sales of capital assets. The Board of Tax Appeals ruled that the loss was deductible in full. The circuit court of appeals affirmed, 108 F. (2d) 753, holding that the loss established by the foreclosure sale was not a loss from a "sale" within the meaning of § 23(j). We granted certiorari, 310 U. S. 619, to resolve a conflict of the decision below with that of the court of appeals for the second circuit in *Commissioner* v. *Electro-Chemical Engraving Co.*, 110 F. (2d) 614.

It is not denied that it was the foreclosure sale of respondents' interest in the land purchased by the syndicate for profit, which finally liquidated the capital investment made by its members and fixed the precise amount of the loss which respondents seek to deduct as such from gross income. But they argue that the "losses from sales" which by § 23(j) are made deductible only to the limited extent provided by § 117(d) are those losses resulting from sales voluntarily made by the taxpayer, and that losses resulting from forced sales like the present not being subject to the limitations of § 117(d) are deductible in full like other losses under § 23(e)(2).

To read this qualification into the statute respondents rely on judicial decisions applying the familiar rule that a restrictive covenant against sale or assignment refers to the voluntary action of the covenantor and not to transfers by operation of law or judicial sales *in invitum*. See *Guaranty Trust Co.* v. *Green Cove & M. R. Co.*, 139 U. S. 137; *Gazlay* v. *Williams*, 210 U. S. 41; *Riggs* v. *Purssell*, 66 N. Y. 193. But here we are not concerned with a restrictive covenant of the taxpayer, but with a sale as an effective means of establishing a deductible loss for the purpose of computing his income tax. The term sale may have many meanings, depending on the context, see Webster's New International Dictionary. The meaning here depends on the purpose with which it is used in the statute and the legislative history of that use. Hence the respondents argue that the purpose of providing in the 1934 Act for a special treatment of gains or losses from capital assets was to pre-

vent tax avoidance by depriving the taxpayer of the option allowed to him by the earlier acts, to effect losses deductible in full by sales of property at any time within two years after it was acquired, which until held for that period was not defined as a capital asset, § 208 Revenue Act of 1924, 43 Stat. 253; § 208 Revenue Act of 1926, 44 Stat. 19, and § 101 of the Revenue Act of 1928, 45 Stat. 811.

It is said that since losses from foreclosure sales not within the control of the taxpayer are not within the evil aimed at by the 1934 Act, they must be deemed to be excluded from the reach of its language. To support this contention respondents rely on the report of the Ways and Means Committee submitting to the House the bill which, with amendments not now material, became the Revenue Act of 1934. The Committee in pointing out a "defect" of the existing law said: "Taxpayers take their losses within the two year period and get full benefit therefrom and delay taking gains until the two-year period has expired, thereby reducing their taxes". H. Rept. 704, 73d Cong., 2d Sess., pp. 9 and 10.

But the treatment of gains and losses from sales of capital assets on a different basis from ordinary gains and losses was not introduced into the revenue laws by the 1934 Act. That had been a feature of every revenue law beginning with the Act of 1921, 42 Stat. 227, and each had defined as capital losses "losses from sales or exchanges of capital assets". The 1934 Act made no change in this respect but for the first time it provided that "capital assets" should include all property acquired by the taxpayer for profit regardless of the length of time held by him and that capital gains and losses from sales of capital assets should be recognized in the computation of taxable income according to the length of time the capital assets are held by the taxpayer, varying from 100% if the capital asset is held for not more than a year to 30% if it is held more than ten years. § 117(a). Finally, for the first time, the statute provided that capital losses in excess of capital gains should be deducted from ordinary income only to the extent of $2,000. Thus by treating all property acquired by the taxpayer for profit as capital assets and limiting the deduction of capital losses in the manner indicated, the Act materially curtailed the advantages which the taxpayer had previously been able to gain by choosing the time of selling his property.

The definition of capital losses as losses from "sales" of capital assets, as we have pointed out, was not new. As will presently appear, the legislative history of this definition shows that it was not chosen to exclude from the capital assets provisions losses resulting from forced sales of taxpayers' property. And, if so construed, substantial loss of revenue would result under the 1934 Act, whose purpose was to avoid loss of revenue by the application of the capital assets provisions. In drafting the 1934 Act the Committee had before it proposals for stabilizing the revenue by the adoption of the British system under which neither capital gains nor losses enter into the computation of the tax. In declining to follow this system in its entirety the Committee said: "It is deemed wiser to attempt a step in this direction without letting capital gains go entirely untaxed". It accordingly reduced the tax burden on capital gains progressively with the increase of the period up to ten years, during which the taxpayer holds the capital asset, and permitted the deduction, on the same scale, of capital losses, but only to the extent that there are taxable capital gains, plus $2,000. In thus relieving capital gains from the tax imposed on other types of income, it cannot be assumed, in the absence of some clear indication to the contrary, that Congress intended to permit deductions in full of losses resulting from forced sales of the taxpayers' property, from either capital gains or ordinary gross income, while taxing only a fraction of the gains resulting from the sales of such property. See *White* v. *United States*, 305 U. S. 281, 292; *Helvering* v. *Inter-Mountain Life Ins. Co.*, 294 U. S. 686, 689, 690.

The taxation of capital gains after deduction of ~~taxable~~ capital losses on a more favorable basis than other income, was provided for by § 206 of the 1921 Revenue Act, as the means of encouraging profit-taking sales of capital investments, H. Rept. No. 350, 67th Cong., 2d Sess., p. 8. *Burnet* v. *Harmel*, 287 U. S. 103, 106. In this section, as in later Acts, capital net gain was defined as "the excess of the total capital gain over the sum of capital deductions, and capital losses"; capital losses being defined as the loss resulting from the sale or exchange of capital assets. In submitting the proposed Revenue Act of 1924, the House committee pointed out that the 1921 Act contained no provision for limiting deduction of capital losses where they exceeded the amount of capital gains. H. Rept. No. 179, 68th Cong., 1st Sess., p. 14. This was remedied by providing in § 208(c)

that the amount by which the tax is reduced on account of a capital loss shall not exceed 12½% of the capital loss. In commenting on this provision the Committee said, p. 10: "If the amount by which the tax is to be increased on account of capital gains is limited to 12½% of the capital gain it follows logically that the amount by which the tax is reduced on account of capital losses shall be limited to the 12½% of the loss." This provision was continued without changes now material until the 1934 Act. § 208(c) in the 1924 and 1926 Acts; § 101(b) in the 1928 and 1932 Act, 47 Stat. 191.

Congress thus has given clear indication of a purpose to offset capital ~~assets~~ gains by losses from the sale of like property and upon the same percentage basis as that on which the gains are taxed. See *United States* v. *Pleasants,* 305 U. S. 357, 360. This purpose to treat gains and deductible losses on a parity but with a further specific provision provided by § 117(d) of the 1934 Act, permitting specified percentages of capital losses to be deducted from ordinary income to the extent of $2,000, would be defeated in a most substantial way if only a percentage of the gains were taxed but losses on sales of like property could be deducted in full from gross income. This treatment of losses from sales of capital assets in the 1924 and later Acts and the reason given for adopting it afford convincing evidence that the "sales" referred to in the statute include forced sales such as have sufficed, under long accepted income tax practice, to establish a deductible loss in the case of non-capital assets. Such sales can equally be taken to establish the loss in the case of capital assets without infringing the declared policy of the statute to treat capital gains and losses on a parity.

We can find no basis in the language of the Act, its purpose or its legislative history, for saying that losses from sales of capital assets under the 1934 Act, more than its predecessors, were to be treated any differently whether they resulted from forced sales or voluntary sales. True, courts in the interpretation of a statute have some scope for adopting a restricted rather than a literal or usual meaning of its words where acceptance of that meaning would lead to absurd results, *United States* v. *Katz,* 271 U. S. 354, 362, or would thwart the obvious purpose of the statute, *Haggar* v. *Helvering,* 308 U. S. 389. But courts are not free to reject that meaning where no such consequences follow and where, as here, it appears to be consonant with

the purposes of the Act as declared by Congress and plainly disclosed by its structure.

It is not without significance that Congress, in the 1934 Act, enlarged the scope of its provisions relating to losses from sales of capital assets by including within them losses upon the disposition of the taxpayer's property by methods other than sale and without reference to the voluntary action of the taxpayer. It thus treats as losses from sales or exchanges the loss sustained from redemption of stock, § 115(c), retirement of bonds, § 117(f), losses from short sales, § 117(e)(1), and loss sustained by failure of the holder of an option to exercise it, § 117(e)(2), although none of these transactions involves a loss from a sale. See *McClain* v. *Helvering*, No. 55, decided this day.

The scope of the capital loss provisions was still further enlarged by § 23(k)(2) of the Revenue Act of 1938, 52 Stat. 447, which provides that if securities, which are capital assets, are ascertained to be worthless and are charged off within the taxable year the loss, with an exception not now material, shall be considered as a loss arising from a sale or exchange. These provisions disclose a consistent legislative policy to enlarge the class of deductible losses made subject to the capital assets provisions without regard to the voluntary action of the taxpayer in producing them. We could hardly suppose that Congress would not have made provision for the like treatment of losses resulting from a forced sale of the taxpayer's property acquired for profit either in the 1934 or 1938 Act, if it had thought that the term "sales or exchanges" as used in both acts did not include such sales of the taxpayer's property.

Respondents

~~Petitioners~~ also advance the argument, sustained in *Commissioner* v. *Freihofer*, 102 F. (2d) 787, that the definitive event fixing respondents' loss was not the foreclosure sale but the decree of foreclosure which ordered the sale and preceded it. But since the foreclosure contemplated by the decree was foreclosure by sale and the foreclosed property had value which was conclusively established by the sale for the purposes of the foreclosure proceeding, the sale was the definitive event establishing the loss within the meaning and for the purpose of the revenue laws. They are designed for application to the practical affairs of men. The sale, which finally cuts off the interest of the mortgagor and is the means for determining the amount of the deficiency judgment against him is a means